

CODE MODIFICATION PROPOSAL No. 0044
"Revised Emergency Cash-out & Curtailment Arrangements"
Version 3.0

Date: 31/10/2005

Proposed Implementation Date: 01/10/2005

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)

Transco NTS* requests that this Modification Proposal* be deemed to be an Urgent Modification Proposal* by the Authority* on the basis Transco NTS believes that the proposed revisions to the cash-out arrangements, which apply during a Gas Supply Emergency*, should be implemented prior to Winter 2005/06.

Transco NTS is concerned that the current cash-out arrangements, which apply during a Gas Supply Emergency, do not provide the most appropriate incentives on Users* to make suitable provision to avoid entering into a Gas Supply Emergency situation, or to minimise the extent or duration of such a Gas Supply Emergency. This Modification Proposal seeks to provide appropriate incentives on Users in this area.

The Authority has expressed concern in relation to "price sensitive" deliveries to the UK gas market and also questioned whether the currently envisaged cash-out prices that might apply in respect of Gas Days* during a Gas Supply Emergency* would provide sufficient incentive to ensure such deliveries.

In order to provide sufficient time for the industry to respond to the changed incentives that would apply for this coming Winter, Transco NTS believes that the decision on this Modification Proposal should be provided as a matter of urgency.

In its decision letter for Modification Proposal 0021, the Authority noted that it would be minded to grant urgent status to any Modification Proposal which sought to address the short term issues they noted with respect to emergency cash-out arrangements due to the important nature of these arrangements for the winter. This Modification Proposal seeks to do this and better facilitates the relevant objectives and Transco NTS hence request that the Authority grants urgent status to this Modification Proposal.

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

Where capitalised words and phrases are used within this Modification Proposal, those words and phrases shall usually have the meaning given within the Uniform Network Code (unless they are otherwise defined in this Modification Report). Key UNC defined terms used in this Modification Proposal are highlighted by an asterisk (*) when first used. This Modification

Proposal, as with all Modification Proposals, should be read in conjunction with the prevailing UNC. For the purposes of this Modification Proposal, “Gas Deficit Emergency” or “GDE” shall mean a Network Gas Supply Emergency Gas Deficit Emergency*.

Words and phrases marked with a double asterisk (**), when first used, are new UNC defined terms that are proposed in the legal text relating to this Modification Proposal.

Transco NTS raised Uniform Network Code Modification Proposal 0021 “Revision of the Emergency Cash-Out Arrangements” in June 2005. The Modification Proposal was rejected by the Authority. In the Authority’s decision letter, they expressed support for the principles of the Modification Proposal but felt they were not in a position to approve the Modification Proposal due to the “serious concerns about the adequacy of the consultation process and in particular whether all of the relevant issues and effects were set out sufficiently clearly and addressed so that respondents and the Modification Panel* could properly consider and comment on the proposal.” In addition, the decision letter set out a number of additional elements that the Authority thought would merit further consideration in any further Modification Proposal in this area. The decision letter encouraged Transco NTS and the industry to bring forward further Proposals for this Winter given the importance of these arrangements.

This Proposal represents an alternative to Modification Proposal 0021 taking into account User concerns expressed as part of the consultation process in relation to Modification Proposal 0021 and also seeking to address issues set out in the Authority’s decision letter relating to Modification Proposal 0021.

In summary, this Modification Proposal builds upon Modification Proposal 0021 by:

- Maintaining the proposed amendment of the setting of the Emergency* cash-out prices from the prevailing single price of the 30 day average System Average Price* to dual prices set at the point of market suspension;
- Maintaining the introduction of a new Emergency Curtailment Quantity** title trade and associated 'trade' payment but extending this to a wider population of loads than just Interruptible* load. This Proposal now covers all System Exit Points* except those which include NDM Supply Point Components* or Priority Supply Points*;
- Introducing a new disputes resolution process for the Emergency Curtailment Quantity title trade quantity;
- Clarifying the treatment of the “Over the Counter” Trade Nomination* process during a Network Gas Supply Emergency*;
- Including a requirement for the relevant DNO* (in respect of DN connected load) to calculate its element of the Emergency Curtailment Quantity and pass this information to Transco NTS;
- Make information regarding each relevant Transporter’s element of the Emergency Curtailment Quantity available to Users after the Gas Day to support dispute process including information describing the basis of the methodology used to calculate each element of the Emergency Curtailment Quantity.

These additional; features and clarifications are designed to address concerns raised with the content of Modification Proposal 0021. The Modification Proposal is discussed in more detail below.

This Modification Proposal seeks to:

1. Amend the setting of the cash-out prices applicable during a Gas Supply Emergency from the prevailing single price of the 30 day average System Average Price to dual prices set at the point of market suspension pursuant to the current provisions of UNC TPD Section Q4.1.1:

- a. the cash-out price for Users with a negative Daily Imbalance* will be set to the System Marginal Buy Price* prevailing on the day the GDE commenced; and
- b. the cash-out price for Users with a positive Daily Imbalance* will be set to the System Average Price prevailing on the day the GDE commenced.

Concerns relating to cash-out prices were raised within the Ofgem “Cash-Out Review Working Group” (CORWG), which recognised that the creation of the Safety Monitors* and the potential for a breach of those Safety Monitors to trigger a Gas Supply Emergency had made the potential of a GDE more predictable; by giving Users time to respond and create appropriate price signals leading up to the declaration of a GDE. During CORWG discussions it was noted that the current arrangements might not appropriately incentivise Users to take all actions that could be considered prudent prior to the commencement of a Gas Supply Emergency*.

One of the principle outcomes of CORWG discussions, to date, was the recognition that appropriate incentives were required to encourage Users to take appropriate actions through which a GDE might be avoided, or, its duration or extent reduced. As a result of the ongoing CORWG review, Transco NTS has considered the next steps that could be taken prior to the coming 2005-2006 Winter.

Any change to the cash-out price applicable during a GDE should ensure that Users do not have a financial incentive to withhold gas, i.e. the cash-out price for Users with a positive Daily Imbalance should fairly reward those providing gas to assist efficient management of the Gas Deficit Emergency, and ensure that Users have an appropriate financial incentive to offer demand-side response. Transco NTS believes that the cash-out price for Users with a negative Daily Imbalance should reflect the marginal value of demand response. This is important to provide appropriate incentives for Users to cover their short positions. A single cash-out price cannot reflect both these values and hence dual cash-out pricing may be more appropriate.

Rather than being based on the average of the System Average Prices for the previous 30 days, Transco NTS believes that the cash-out price applicable during a GDE for those Users with a negative Daily Imbalance should be set to the System Marginal Buy Price that is prevailing at the commencement of a GDE. Transco NTS believes that the setting of the cash-out price applicable during a GDE on this basis would provide the Users with signals that are likely to be more reflective of the actual market conditions immediately prior to a GDE.

Users should be encouraged to deliver and, where appropriate, provide demand-side response, in order to alleviate the extent and duration of the GDE. For example, where Users have a positive Daily Imbalance as a consequence of their actions to maximise beach deliveries or, by responding to GDE demand reduction notices, then these Users should be appropriately rewarded. Thus Transco NTS considers that the cash-out price for a User with a positive Daily Imbalance should be set at the System Average Price at the time immediately prior to the start of the GDE. Transco NTS believes that if implemented, this Modification Proposal would better align the cash-out prices applicable during a GDE to those market prices prevailing at the commencement of a GDE.

The Authority, in its decision letter, reflected concerns raised by respondents in relation to Modification Proposal 0021, which had a similar marginal price proposal to that set out above. These related, in our understanding, to the impact of small quantity trades having the ability to set high marginal prices for a long emergency period and secondly to the read across to discussions and previous Authority statements on electricity cash-out prices.

We have not included any mechanism for a more aggregated marginal approach incorporating either averaging of a number of trades or “de minimis” cash-out prices in this Modification Proposal for the following reasons:

- The gas cash out mechanism for non-emergency periods is already based upon a marginal calculation methodology. Introducing an aggregated marginal price methodology during emergency periods only would mean that different regimes would apply for non-emergency and emergency periods. We believe that this could result in unintended consequences and note that this concurs with Ofgem’s view expressed in its decision letter on BSC Modification Proposal P135 (Marginal System Buy Price during periods of Demand Reduction) where it stated that ‘...through having two regimes in place for the calculation of Energy Imbalance Prices there is scope for perverse incentives to exist.’ The incentives and impacts of two different cash out regimes would need to be fully assessed and discussed.
- Prior to entering an emergency period, Transco NTS will accept all economic and efficient offers on the OCM. In assessing the economics and efficiencies of a particular offer, Transco NTS will consider whether the quantity of that action will have a discernible positive impact on the supply/demand position. Thus, a small quantity, high price action may well not be taken, as it would not aid in the overall supply/demand balance position. If there were a number of small quantity actions that could be taken that, in aggregate, would aid the overall Supply & Demand balance position, then Transco NTS would accept them. In these circumstances, it is Transco NTS’s view that, as the highest priced action has helped to resolve the supply/demand imbalance, it is appropriate for it to set the cash out price.
- In all circumstances, including emergency circumstances, it is essential that cash-out prices provide Users with strong incentives to balance their positions. During stages 2 and 3 of an emergency, Users will be able to enter into OTC trades and submit nominations to Transco NTS, and therefore cash-out prices at these times not only provide incentives for Users to undertake such trades in order to balance their positions, but also incentives to ensure that gas is physically delivered. This is distinct

from the electricity arrangements where Gate Closure prevents market participants from trading with each other, (as the sole counterparty is the system operator) and there are alternative mechanisms and obligations in place to ensure physical delivery. As such we believe that a 'pure marginal' SMP Buy price is required during a GDE to ensure that no financial benefit can be derived from undertaking a trade at one price, not physically delivering, and being cashed out at a discounted price due to any aggregation at the margin.

- We note Ofgem's view that the issues around small volumes of gas setting the cash out price are less significant than they are in electricity due to the longer balancing period. Additionally we believe that the nature (i.e. the number of actions and the timescales associated with delivery) of gas balancing actions minimise the risks of a small volume balancing action inappropriately setting the cash out price.
- From our experience of the electricity industry, cash out price proposals have resulted in significant debate and discussion as (amongst other things) there are a number of ways of calculating either de-minimis quantities or a subset of trade quantities all of which need to be assessed for their impact and incentive properties. We believe that any future proposed modification on electricity cash out prices should include consideration of this area, but do not believe that this is a pre-requisite for this gas cash out modification, for the reasons outlined above.
- We note the Authority's and industry concerns, and believe that if any market participant were to bring forward a proposal to develop an aggregated or "de minimis" marginal price then this should be considered on its own merits and would require significant development and discussion with the industry.

Therefore, we have not proposed a solution incorporating any aggregation or de-minimis limits within the cash out calculation methodology, and we believe that our proposed pricing element to this Modification Proposal better meets the relevant objectives.

Trading Arrangements & Clarification of "Over the Counter" Trade Nomination process operation

If a marginal cash-out price applies to those Users that are short in a GDE then it should be possible for such Users to trade out their imbalances and hence all Trade Nominations at all stages of a Network Gas Supply Emergency will be accepted. For the avoidance of doubt, UNC TPD Section C5 will continue to apply during a GDE. This change will effectively remove the ability of Transco NTS not to take into account "OTC" trades in a GDE.

2. Introduction of a new Emergency Curtailment Quantity title trade and associated 'trade' payment

The second element of this Modification Proposal is seeking to assign the quantities of gas associated with Emergency Curtailment actions undertaken by Transco NTS in a GDE (including a Potential GDE) as a Trade Nomination between Transco NTS and each User. Emergency Curtailment covers an instruction from the relevant Transporter to reduction or discontinuance of offtake of gas at any relevant System Exit Point. Relevant System Exit Points are described later in this section.

In the event of a potential or actual GDE, Emergency Curtailment would be used in an attempt to reach a system supply & demand balance i.e. removal of the deficit. This could result in a scenario where a User, which was short of gas going in to an Emergency or Potential Emergency, might have its potential daily imbalance reduced because of the demand reduction associated with Interruption or Firm load shedding by the action of the relevant Transporter calling such Emergency Curtailment. This might result in limited cost targeting of those Users that contributed towards an emergency, which might weaken the financial incentive to contract for adequate supplies and demand response. Associating a title trade with Emergency Curtailment would, to some extent, correct this lack of cost targeting.

If a trade were associated with the Emergency Curtailment Quantity, a User that has a negative Daily Imbalance prior to an emergency would be financially exposed at the System Marginal Buy Price to the full extent of its envisaged Daily Imbalance position prior to the invoking of Emergency Curtailment. A User that was in balance or had a positive Daily Imbalance prior to an emergency would retain a similar envisaged Daily Imbalance position following the invoking of Emergency Curtailment.

For each User, the Emergency Curtailment Quantity would be calculated as the aggregate quantity of Emergency Curtailment occurring as a result of a potential or actual GDE at the relevant System Exit Points less any quantity of User commercial “interruption” at the same System Exit Points notified to the relevant Transporters* prior to the Emergency Curtailment occurring.

For each day in an Emergency the Emergency Curtailment Quantity (ECQ) will be expressed as a Daily Quantity (kWh) for each User and will be the sum of the elements provided by each relevant Transporter.

The methodology each Transporter may use to calculate its element of the Emergency Curtailment Quantity is discussed later in this section.

Relevant System Exit Points

A key issue is to which loads this Emergency Curtailment Quantity title trade applies to.

Transco NTS understands that the key issue in regard to the clarity of Modification Proposal 0021 was the term “Emergency Interruption” which was used in conjunction with the trade quantity aspect of the Modification Proposal. This term meant that the trade quantity adjustment applied solely to Interruption as an Emergency Step* i.e. curtailment of the offtake of gas at Interruptible Supply Points*.

The Authority in their decision letter noted that they felt Modification 0021 “arbitrarily drew a distinction between (currently defined) interruptible and firm customers in relation to the incentives that Users face regarding ex ante contracting for demand response. Ofgem considers that this aspect of the proposal is contrary to the efficient and economic operation of the pipeline system”. We have considered whether there is a different definition of the loads to which the

trade quantity aspect of the Modification Proposal will apply to which might better facilitate the relevant objectives.

In response to specific concerns, this Modification Proposal contains a wider definition of Supply Points than Modification Proposal 0021. The key difference is that we propose that the trade quantity should apply to the reduction of the offtake of gas at all System Exit Points other than those which comprise NDM Supply Meter Points* and Priority Supply Points. These excluded loads are protected by the GSMR Safety Monitor under the NEC Safety Case* and it would be inappropriate to incentivise a demand response at such Supply Points as it would not be possible to accept or validate a market based demand response. Therefore we believe that setting the threshold excluding these loads is an appropriate one.

Trade and Trade Payment Arrangements

To ensure transparency and consistency with other Eligible Balancing Actions*, Emergency Curtailment during a GDE (including a Potential GDE) would represent a Market Balancing Action*, only for invoicing and neutrality purposes, and thus any payment for such actions should be funded from the energy element of Balancing Neutrality*.

For the avoidance of doubt, any amounts payable by Transco NTS to Users for the Emergency Curtailment Quantity trade shall not be included in the calculation of the System Marginal Buy Price, the System Marginal Sell Price or the System Average Price. Transco NTS will not pay Balancing Charges*, Balancing Neutrality Charges*, Scheduling Charges* or Daily Imbalance Charges* as a result of the Emergency Curtailment Quantity transactions occurring.

In addition to the Trade Nominations in respect of the Emergency Curtailment Quantity, it is also proposed that for those occurrences of Interruption in a GDE, the Users would receive payment based on the Emergency Curtailment Quantity multiplied by a price determined as the simple average of the System Average Prices for the 30 Days prior to the commencement of the GDE.

This would result in a payment from Transco NTS to each User in respect of the aggregate quantity of gas that User would have offtaken but for the Emergency Curtailment occurring during a GDE. The Emergency Curtailment Quantity would be calculated to offset the gas deficit in a GDE (including a Potential GDE) and the net Daily Imbalance* of all Users should be equal and opposite to the aggregate imbalance of a new Transco NTS 'Emergency Curtailment Manager' account.

Each Transporter would be responsible for generating an estimate of its element of the Emergency Curtailment Quantity, by User, in relation to the Emergency Curtailment actions taken by that Transporter during a potential or actual GDE. Transco NTS will aggregate each Transporter's element of the ECQ to generate a single Emergency Curtailment Quantity for each User for the day.

Shared Supply Meter Points*

For Shared Supply Meter Points*, the Registered Users (or agent on behalf of such Registered Users) will be required to provide a default User allocation method that applies unless Users have called User “interruption”. If no default User allocation method is available the relevant Transporter default allocation will be used.

Information Flow

For the purposes of implementing this Modification Proposal, Transco NTS would need access to the Emergency Curtailment Quantity data by User, of each relevant Transporter, in its role as residual system balancer. Transco NTS as residual system balancer would be responsible for collating the component elements, supplied by each relevant Transporter including the Transco NTS element, of the Emergency Curtailment Quantity. Transco NTS will then calculate the Emergency Curtailment Quantity as the sum of the above supplied elements by User, calculate the price and initiate the Trade Nominations and corresponding payments.

As noted above, the Modification Proposal places an obligation on all relevant Users at Shared Supply Meter Points to provide the division method for the Emergency Curtailment Quantity for the relevant Transporter not more than one hour after relevant actions have been initiated.

The Modification Proposal places an obligation on all relevant Transporters to calculate the Emergency Curtailment Quantity for all relevant System Exit Points and pass the data, aggregated by User, on to Transco NTS as soon as is reasonably practical after Emergency Curtailment** has been initiated.

The Modification Proposal will also place an obligation on all relevant Transporters to pass the User specific data on to the relevant User along with the basis for the calculation as soon as is reasonably practical after the day that Emergency Curtailment has been initiated and in any case no later than D+4.

Calculation of the Emergency Curtailment Quantity

A key issue to the functioning of the process will be the process by which each relevant Transporter calculates its element of the ECQ. As noted in the Authority’s decision on Modification Proposal 0021, many respondents would like to see the ECQ calculation method set out in the Uniform Network Code. We would concur with the principle of such a view in that Users would need to understand the process by which the relevant Transporter would calculate its element of the ECQ, however, we would concur with Ofgem’s view as set out in the Authority’s decision letter that consideration of whether this should be incorporated into the UNC is a medium term issue, therefore we have not included this aspect in this Modification Proposal.

We are however keen that Users understand the processes used and hence we will be publishing our view of the processes we believe the relevant Transporter’s should use alongside this Modification Proposal such that Users can consider this in their assessment of the Modification. We believe this is the optimal way forward as it would allow Users to comment on such a methodology and we will set up industry sessions to discuss the ECQ processes during the

consultation process. We believe that a single methodology, comprising a number of distinct steps, covering all relevant System Exit Points could be applied by all Transporters.

Even without the formal inclusion of the ECQ methodology, we believe that this Modification Proposal better meets the relevant objectives, as it requires the relevant Transporter to provide a best estimate of its element of the ECQ. The Modification Proposal provides that information is sent to the User by each relevant Transporter to inform them how its element of the Emergency Curtailment Quantity was assessed and it includes a quantity dispute process should the User believe there was a better estimate that could have been used. We believe this is significantly better than the status quo of no quantity adjustment at all in the Emergency arrangements.

Further Emergency Curtailment and Restoration**

In the event of the NEC declaring a potential or actual GDE, the requirement for Emergency Steps* to include Emergency Curtailment at a number of System Exit Points may be identified. If the Emergency Steps do not avert or reduce the probability of the GDE or the probable scale of the GDE then further Emergency Steps will be taken. In the event of further Emergency Curtailment occurring, each relevant Transporter should provide revised ECQ elements to Transco NTS. Transco NTS will then initiate further title trades to reflect any increased quantities.

Should Emergency Steps avert the probability of a GDE and the restoration of the offtake of gas at all or a number of System Exit Points is feasible without increasing the probability of a GDE then such restoration will be initiated. In the event of such restoration occurring, revised ECQ elements should be provided to Transco NTS by each relevant Transporter. Transco NTS will then initiate further title trades to reflect restoration i.e. reduced quantities.

On any Day in which restoration of Emergency Curtailment occurs at one or more System Exit Points, then each User that has a revised Emergency Curtailment Quantity due to restoration will be required to authorise Transco NTS to make an Acquiring Trade Nomination on behalf of the User, and Transco NTS will make a corresponding Disposing Trade Nomination.

Impact and notification of User “interruption”

In the event of the NEC* declaring a GDE, Emergency Curtailment may occur at a System Exit Point that has already been commercially “interrupted” for the relevant Gas Day (or Gas Days) by a User to ensure that the System Exit Point does not restart taking gas. This process is known as ‘trumping’. Given that any revised emergency arrangements should lead to greater incentives on Users to contract for and action commercial “interruption” as well as contracting for greater supply quantities, it is the intent of this Proposal that any notified User commercial “interruption” should not count towards the Emergency Curtailment Quantity. User “interruption” must be notified to the relevant Transporter (UNC TPD Section G6.6.5) by the use of a “P70” form and aggregate User “interruption” is already calculated from this data.

As part of this Modification Proposal the process for the notification of User commercial “interruption” (UNC TPD Section G6.6.5) will be expanded to enable Users to notify the

relevant Transporter of commercial “interruption” at both Interruptible and relevant Firm System Exit Points as covered by the definition of relevant System Exit Points. This will be facilitated by the introduction of an additional “P70 Firm” form for relevant Firm System Exit Points while the prevailing “P70” form will continue to be applicable for Interruptible System Exit Points. This process will apply at all stages of a Potential or actual GDE.

In order for the process to work effectively it is important that there is clarity in regard to the notification of User “interruption” at both Interruptible and relevant Firm System Exit Points. A User should notify Transco NTS of User “interruption” only if the Supply Point reduces or stops the offtake of gas under any commercial arrangement with that User. If a User offers demand reduction via a physical or locational action on the “OCM” then the initiated demand reduction should be covered by a “P70” or “P70 Firm”. If a User “interrupts” a Shared Supply Meter Point* then it should not issue a “P70” if it intends to act as the User for that Supply Point* under other contractual arrangements such as the purchase of gas by the end-consumer.

Quantity dispute process

In the Authority’s decision letter on Modification Proposal 0021, it noted that some Users had commented that a disputes process would be helpful for the Emergency Curtailment Quantity aspect of the Modification Proposal. We have therefore included in this Modification Proposal a dispute process for the Emergency Curtailment Quantity. For this purpose and given the urgent request we have made with this Modification Proposal, we have built the Modification Proposal on the existing claims process which is in place for parties who have a positive Daily Imbalance going into an emergency. Clearly, the disputes process is an issue which can be developed over time through further Modification Proposals in the light of experience. However we believe introducing a disputes process based on one which is already functioning under the Uniform Network Code will better facilitate the relevant objectives.

Where a User believes that its Emergency Curtailment Quantity has been incorrectly calculated, a claims process may be initiated.

- Transco NTS will, in consultation with the UNC Committee*, appoint an appropriately qualified person as "claims reviewer" to review each claim.
- This claims reviewer will advise Transco NTS whether or not the calculated Emergency Curtailment Quantity appears to the claims reviewer to be justified and (if not) what the Emergency Curtailment Quantity (in the claims reviewer's opinion) should be.
- If the claims reviewer advises of a lower Emergency Curtailment Quantity, then the User will be required to pay Transco NTS an amount determined by multiplying the Emergency Curtailment Trade Price** by the difference between the calculated Emergency Curtailment Quantity and determined Emergency Curtailment Quantity.
- If the claims reviewer advises of a higher Emergency Curtailment Quantity, then Transco NTS will be required to pay the User an amount determined by multiplying the Emergency Curtailment Trade Price** by the difference between determined Emergency Curtailment Quantity and the calculated Emergency Curtailment Quantity.

- In addition, there would be a requirement to adjust the relevant User's imbalance account for the Gas Day in question.
- Either party may appeal the claims reviewer's decision to the Authority.

For the avoidance of doubt, there will be no price claims process in relation the Emergency Curtailment Quantity trade as Transco NTS believes that such a process would have a detrimental impact on the intent of this Modification Proposal in regard to the generation of incentives.

Users would be able to initiate the disputes process referred to above prior to having to pay any Balancing Charges* that may arise as a result of the calculated Emergency Curtailment Quantity.

Consequences of not implementing this Modification Proposal

- Anything other than the application of the System Marginal Buy Price and the maintaining of pre-emergency Daily Imbalances in a GDE would not fully incentivise delivery against all residual balancer Market Balancing Actions taken prior to the declaration by the NEC of a GDE.
- The prevailing cash-out arrangements might incentivise behaviour that might lead to the prolonging of an emergency.
- Potential perverse incentives for Users who are short of gas going into an emergency would remain.
- Users would have a weaker incentive to contract for demand response.
- Potential Security of Supply benefits would not be realised.

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 that this Modification Proposal, if implemented, would better facilitate the following relevant objective as set out in the Transco NTS gas transporter's licence:

The Modification Proposal should ensure that Users continue to be incentivised prior to, and during an emergency, to satisfy their contracted demands. Increased security of supply should lead to more efficient utilisation of the pipeline system and hence Transco NTS believes that the Modification Proposal will better facilitate relevant objective 1b); the coordinated, efficient and economical operation of the combined pipeline system.

In respect of paragraph 1.d): Transco NTS anticipates that by targeting cost during a GDE, Users will be encouraged to take appropriate actions through which a GDE might be avoided. Such actions might promote greater and more effective competition between Users and Suppliers*, and as a result might improve security of supply.

Advantages of the Modification Proposal

Transco NTS believes that the Modification Proposal;

- Introduces appropriate incentives through which Users are encouraged to make suitable provisions to avoid entering into a Potential Network Gas Supply Emergency situation or, minimize the extent or duration of such a GDE.
- Provides greater incentives for Users and Suppliers to manage their own portfolios and supply obligations.
- Ensures that the correct responsibilities and liabilities are in place to ensure that demand is managed appropriately, therefore may reduce the risk of a GDE.
- Ensures that Users do not have a financial incentive to withhold gas as a result of the GDE cash-out price determination.
- The above advantages should have a positive effect on security of gas supply

Disadvantages of the Modification Proposal

It is recognised that the Modification Proposal adds some additional complexity to the commercial arrangements.

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

Transco NTS recognises that the prevailing emergency cash-out arrangements may have an adverse impact on the likelihood of price sensitive supplies (interconnector, LNG importation) continuing to be delivered in a potential or actual emergency.

Transco NTS believes that the prevailing emergency cash-out arrangements also generate little financial incentive to action demand response as the financial exposure created by a short position and a neutral cash-out price would be expected to be less than the costs associated with the quantity of demand response that would balance a User's portfolio.

Transco NTS believes that end-consumers would value demand response at a level significantly above 30-day average System Average Price*. Given that the potential 1-in-50 annual quantities of demand and the expected supply level for the coming winter indicates a requirement for increased demand-side response, Transco NTS believes that there is insufficient financial incentive to meet the Supplier's licence obligation to maintain supplies in a 1:50 winter to domestic users.

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

a) implications for operation of the System:

Users should be encouraged to deliver and, where appropriate, provide demand-side response, in order to alleviate the extent and duration of the emergency. This alleviation could be considered as a beneficial implication for the operation of the Total System*.

1. Setting of emergency cash-out prices - We do not anticipate any adverse implications in respect of the operation of the Total System.

2. Introduction of a new Emergency Curtailment Quantity trade and associated payment – We do not anticipate any adverse implications in respect of the operation of the Total System.

The price payable in respect of any Emergency Curtailment Quantity will have no impact on the order in which Market Balancing Actions are taken and Emergency Curtailment in an emergency will not be undertaken in preference to Market Balancing Actions. Once an emergency has been declared, Transco NTS will be acting under instruction of the NEC and will use all available tools, Market Balancing Actions or otherwise to manage the Potential (or actual) Network Gas Supply Emergency in accordance with licence obligations and statutory obligations.

b) development and capital cost and operating cost implications:

Transco NTS has identified minimal development and operational costs.

c) extent to which it is appropriate to recover the costs, and proposal for the most appropriate way to recover the costs:

Additional costs will impact on the “SO Incentives” and will be recovered via the “NTS SO Commodity Charge”.

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

No such consequences have been identified.

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

No such consequences have been identified.

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

The association of a trade for any Emergency Curtailment Quantity could be facilitated by the creation of an “Emergency Curtailment Manager” (ECM) account on UK Link. This account would be used to generate the trades on a User aggregated basis. Each User would be deemed to have completed the trade with the ECM entering the Disposing Trade Nomination* on behalf of each User. The ECM account would mirror the balancing operator account in that it would not attract Daily Imbalance Charges and would not be part of the Balancing Neutrality process.

The introduction of a disputes process may require the establishment of new Invoice Items* on the Energy Balancing Invoice*.

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

If implemented this Modification Proposal may introduce incentives which Users may view as significant enough to require putting in place appropriate arrangements and contracts, prior to the coming winter, through which the risk of incurring potential increases in cash-out costs might be mitigated.

Interruption and shedding of Firm loads during an Emergency are processes that a User must already facilitate if required. The Emergency Curtailment Quantity will also be facilitated through existing arrangements and hence no additional administrative or operational costs are envisaged.

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

Draft legal text for this Modification Proposal is set out below. The proposer does not at this stage anticipate amending the draft legal text below, but reserves the right to do so where any errors or omissions are identified during the consultation period in respect of this Modification Proposal or improvements are suggested by respondents to the consultation in respect of this Modification Proposal which enhance the Modification Proposal or better further the principles of the Modification Proposal.

Draft Legal Text

UNC Modification Proposal Draft Legal Text Revised Emergency Cash-out & Curtailment Arrangements

1. Setting of Emergency Cash-Out prices:

UNC – TPD Section Q

Amend paragraph 4.1.1(b) to read as follows:

“(b) Section C (other than paragraph 5 thereof) will not apply, except to the extent to which Transco NTS may wish to use the Nomination process as a means for Users to communicate with Transco NTS;”

Amend paragraph 4.2.3 to read as follows:

“4.2.3 For the purposes of this paragraph 4.2 ~~the ‘relevant price’ is:~~

- (a) the “relevant price” In respect of paragraph 4.2.2 (a) is the System Average Price determined under Section F1.2.1 or F1.2.2; and
- (b) the “relevant price” in respect of paragraph 4.2.2 (b) is the System Marginal Buy Price as determined under Section F1.2.1 (a) ~~the Value of the arithmetic mean of the System Average Prices determined under Section F1.2.1 or F1.2.2~~

In each case but by reference to the 30 days preceding the Day on which the Network Code Gas Supply Emergency Gas Deficit Emergency started”

2. Emergency Curtailment Quantity title trade and associated payment:

UNC – TPD Section F

Amend paragraph 4.4.2 to read as follows:

- “4.4.2 **“Aggregate System Receipts”** for a Day.....:
- (a)
 - (b)
 - (c)
 - (d)that Day; ~~and~~
 - (e)that Day; and
 - (f) the amounts received by Transco NTS from Users pursuant to Section Q6.2 or Section Q6.3 in respect of Users’ Emergency Curtailment Quantity relating to that Day or any revisions thereto.”

Amend paragraph 4.4.3 to read as follows:

- “4.4.2 **“Aggregate System Payments”** for a Day.....:
- (a)
 - (b)that Day; ~~and~~
 - (c) the amounts payable by Transco NTS to Users pursuant to Section Q6.2 or Section Q6.3 in respect of Users’ Emergency Curtailment Quantity relating to that Day or any revisions thereto”

UNC – TPD Section G

Insert the following as new paragraph 1.20:

“1.20 Reduction of Offtake at Firm Supply Points

1.20.1 Where, in relation to any Firm Supply Point (but without prejudice to Section C in relation to Renominations), the Registered User or supplier:

- (a) exercises (other than pursuant to an instruction from a Transporter pursuant to Section Q) any entitlement to require the consumer to discontinue consuming gas offtaken from the Total System on a Day; or
- (b) having exercised such an entitlement, authorises the consumer to resume such consumption

the Registered User will as soon as reasonably practicable, and in accordance with paragraph 1.20.3, inform the Transporter of the matters set out in paragraph 1.20.2, provided that the Registered User shall use reasonable endeavours to inform the Transporter not more than one hour after such discontinuance and/or not less than one hour before such resumption.

1.20.2 The matters to be informed by the Registered User to the Transporter pursuant to paragraph 1.20.1 are:

- (a) the identity of the Firm Supply Point;
- (b) the time with effect from which the consumer will be required to discontinue, or authorised to resume, consumption; and
an estimate of the amount by which the quantity of gas offtaken will increase or decrease as a result of such discontinuance or resumption.

- 1.20.3 For the purposes of paragraph 1.20.1 the User will give the relevant information to the Transporter by means of telephone or facsimile, unless it has given to the Transporter not less than one month's notice of its intention to give such information by Batch Transfer Communication, in which case such User will give information to the Transporter for the purposes of paragraph 1.20.1 only by Batch Transfer Communication, and will promptly inform the Transporter by telephone or facsimile of the transmission of each such Batch Transfer Communication.
- 1.20.4 Where the Transporter notifies a User that it is unable satisfactorily to access a Batch Transfer Communication transmitted pursuant to paragraph 1.20.3, that User will promptly send to the Transporter by facsimile the information contained in that Batch Transfer Communication.”

UNC – TPD Section Q

Amend paragraph 3.4.1 to read as follows:

- “3.4.1 Where:
- (a)
 - (b)
 - (c)
 - (d)

Where a Transporter has taken Emergency Steps that require the reduction or discontinuance of offtake of gas as set out above, and the Transporter subsequently determines that such reduction or discontinuance of offtake of gas is no longer required or will be no longer required at a certain time, then the Transporter will so notify Users specifying the time (where later than the time of such notification) at which such reduction or discontinuance of offtake of gas is no longer required.

In addition, the provisions of paragraph 6 of this Section Q shall apply following any reduction or discontinuance of offtake of gas pursuant to this paragraph 3.4.1 at any System Exit Point (other than at a System Exit Point which includes an NDM Supply Point Component or at a Priority Supply Point) due to a Network Gas Supply Emergency (other than a Network Gas Supply Emergency Critical Transportation Constraint Emergency).”

Amend paragraph 3.4.5 to read as follows:

- “3.4.5 The relevant provisions of G6 will apply for the purposes of Interruption in a Gas Supply Emergency (including a Potential Network Gas Emergency) or Local Gas Supply Emergency, except that:
- (a) the Transporter shall not be required to give 5 hours' notice of Interruption but may require Interruption as soon as practicable following the Transporter's Interruption Notice;
 - (b) the User may not request an alteration pursuant to Section G 6.8.2 to the Supply Points to be Interrupted;
 - (c) any Day or Days of Interruption pursuant to this Section Q shall not count towards the use of the Interruption Allowance under Section G 6.7.5;
 - (d) the provisions of Section G 6.9 (other than Section G 6.9.2(a)) in respect of a failure to Interrupt shall not apply.

In addition, the provisions of paragraph 6 of this Section Q shall apply following Interruption in a Network Gas Supply Emergency (including a Potential Network Gas Emergency) (other than a Network Gas Supply Emergency Critical Transportation Constraint Emergency or a Potential Network Gas Supply Emergency Critical Transportation Constraint Emergency)."

Amend paragraph 4.1.1 to read as follows:

"4.1.1 In respect of each Day or part of a Day during a Network Gas Supply Emergency Gas Deficit Emergency:

- (a)
- (b)
- (c)
- (d)
- (e)
- (f)
- (g)
- (h); and
- (i) the Transporters may by notice to Users suspend the implementation (as respects all Users) of any of the provisions of Section G (other than paragraph 6.6.5 thereof).

Amend paragraph 4.2.2 to read as follows:

"4.2.2 In respect of each Day during a network gas Supply Emergency Gas Deficit Emergency:

- (a) Transco NTS shall pay to each User who delivered on a Day more gas to the Total System than it offtook on such Day an amount determined as the User's Daily Imbalance multiplied by the relevant price, subject to paragraph 4.2.5;
- (b) each User who offtook on a Day more gas from the Total System than it delivered on such Day shall pay to Transco NTS an amount determined as the User's Daily Imbalance multiplied by the relevant price.

For the purposes of this paragraph 4.2.2, and pursuant to the provisions of paragraph 6.2.1, a User's Daily Imbalance shall include that User's Emergency Curtailment Quantity."

Insert the following as new paragraph 6:

6. EMERGENCY CURTAILMENT

6.1 Definitions

6.1.1 For the purposes of the Code:

- (a) **"Emergency Curtailment"** means either:
 - (i) Interruption due to a Network Gas Supply Emergency (including a Potential Network Gas Supply Emergency) other than a Network Gas Supply Emergency Critical Transportation Constraint Emergency or a Potential Network Gas Supply Emergency Critical Transportation Constraint Emergency; or

- (ii) any reduction or discontinuance of offtake of gas pursuant to paragraph 3.4.1 at any System Exit Point (other than at a System Exit Point which includes an NDM Supply Point Component or at a Priority Supply Point) due to a Network Gas Supply Emergency (other than a Network Gas Supply Emergency Critical Transportation Constraint Emergency);
- (b) “Emergency Curtailment Trade Price” means the value (in pence/kWh) of the arithmetic mean of the System Average Prices determined under Section F1.2.1 or F1.2.2 but by reference to the 30 Days preceding the Day on which the Emergency Curtailment occurred; and
- (c) “Emergency Curtailment Quantity” means, in respect of a User, the quantity of gas calculated by Transco NTS as being the sum of the aggregate quantities of gas (in kWh) which each Transporter reasonably estimates (based on the information available to it at the time of making such estimate) that User would have offtaken from the relevant Transporter’s System at System Exit Points in respect of which Emergency Curtailment has occurred but for the fact that Emergency Curtailment had occurred at those System Exit Points.

6.2 Emergency Curtailment Trade Arrangements

- 6.2.1 In the event that Emergency Curtailment occurs, then each User that has an Emergency Curtailment Quantity authorises Transco NTS to make a Disposing Trade Nomination on behalf of the User, and Transco NTS will make a corresponding Acquiring Trade Nomination, in each case for the User’s Emergency Curtailment Quantity.
- 6.2.2 Transco NTS will pay to each User an amount determined as the User’s Emergency Curtailment Quantity multiplied by the Emergency Curtailment Trade Price.
- 6.2.3 In the event that further Emergency Curtailment is required in respect of a Day, or Emergency Curtailment that had previously occurred in respect of that Day is removed, then Transco NTS shall calculate a revised Emergency Curtailment Quantity for each User based on any updated estimates provided to it by the Transporters, and:
 - (a) where the effect is such that a User’s revised Emergency Curtailment Quantity is greater than the User’s previously calculated Emergency Curtailment Quantity, each such User authorises Transco NTS to make a Disposing Trade Nomination on behalf of the User, and Transco NTS will make a corresponding Acquiring Trade Nomination, in each case for the difference between the User’s revised Emergency Curtailment Quantity and the User’s previously calculated Emergency Curtailment Quantity; and
 - (b) where the effect is such that a User’s revised Emergency Curtailment Quantity is less than the User’s previously calculated Emergency Curtailment Quantity, each such User authorises Transco NTS to make a Acquiring Trade Nomination on behalf of the User, and Transco NTS will make a corresponding Disposing Trade Nomination, in each case for the difference between the User’s previously calculated Emergency Curtailment Quantity and the User’s revised Emergency Curtailment Quantity.
- 6.2.4 In the circumstances set out in:
 - (a) paragraph 6.2.3(a), Transco NTS will pay to the User an amount determined as the difference between the User’s revised Emergency Curtailment Quantity and the User’s previously calculated Emergency Curtailment Quantity multiplied by the Emergency Curtailment Trade Price;

- (b) paragraph 6.2.3(b), the User will pay to Transco NTS an amount determined as the difference between the User's previously calculated Emergency Curtailment Quantity and the User's revised Emergency Curtailment Quantity multiplied by the Emergency Curtailment Trade Price.
- 6.2.5 Transco NTS will not pay Balancing Charges, Balancing Neutrality Charges, Scheduling Charges or Daily Imbalance Charges as a result of Trade Nominations occurring as a result of the operation of paragraphs 6.2.1 or 6.2.3.
- 6.2.6 For the avoidance of doubt, any amounts payable by Transco NTS pursuant to paragraph 6.2.2 or 6.2.4 shall not be included in the calculation of the System Marginal Buy Price, the System Marginal Sell Price or the System Average Price pursuant to Section F1.2 for the Day to which the Emergency Curtailment Quantity relates.
- 6.2.7 Where, following the end of a Day, a User (the "claimant") believes that it ought to have had a different Emergency Curtailment Quantity to that determined pursuant to this paragraph 6 and applicable at the end of the Day in question:
- (a) the claimant may, within such time as Transco NTS shall reasonably require, submit to Transco NTS a claim that it ought to have had a different Emergency Curtailment Quantity, together with details of the basis on which it believes it ought to have had a different Emergency Curtailment Quantity;
- (b) Transco NTS will (in consultation with the UNC Committee) appoint an independent accountant or other appropriately qualified person as "claims reviewer" to review each claimant's claim and advise Transco NTS of whether the claim appears to the claims reviewer to be justified and the Emergency Curtailment Quantity which (in the claims reviewer's opinion) the claimant should have had;
- (c) the claimant shall be required (as a condition to its claim being considered, but subject to the claims reviewer accepting a reasonable obligation of confidence) to provide such information, access to records and cooperation as the claims reviewer shall reasonably require;
- (d) the fees and costs of the claims reviewer shall be paid by Transco NTS and shall be additional Monthly Adjustment Neutrality Costs for the month in which they are paid;
- (e) in the event that either the claimant or Transco NTS disagrees with the claims reviewer's decision, it may refer the matter to the Authority, and the Authority may determine either that the claims reviewer's decision was correct or may direct that a different Emergency Curtailment Quantity to that determined by the claims reviewer should be used; and
- (f) where the claims reviewer advises (or, following a referral by either Transco NTS or the claimant pursuant to paragraph (e), the Authority determines) that the User's Emergency Curtailment Quantity calculated by Transco NTS pursuant to this paragraph 6 was larger or smaller than it ought to have been, then the provisions of paragraph 6.3 shall apply.
- 6.2.8 In respect of any Shared Supply Meter Point, the Registered Users of such Shared Supply Meter Point (or an agent acting on behalf of such Registered Users) shall, not more than one (1) hour after the occurrence of any Emergency Curtailment, notify the relevant Transporter of the proportions in which the relevant Transporter shall allocate between the Registered Users of such Shared Supply Meter Point the quantity of gas that would

have been offtaken at such Shared Supply Meter Point but for any Emergency Curtailment. If no such proportions have been provided, the Transporter shall allocate between the Registered Users of such Shared Supply Meter Point the quantity of gas that would have been offtaken at such Shared Supply Meter Point but for any Emergency Curtailment in proportions based on the Transporter's estimate of the quantity of gas that each Registered User would have offtaken at the Shared Supply Meter Point but for the Emergency Curtailment.

6.2.9 As soon as reasonably practicable after the end of a Day on which Emergency Curtailment occurred (and in event, not later than 20:00 hours on 4th Day after the Day in question), each Transporter shall notify each User of the proportion of that User's Emergency Curtailment Quantity for that Day that relates to System Exit Points on that Transporter's System, together with the methodology used to calculate such proportion.

6.3 Emergency Curtailment Adjustment

6.3.1 Where the provisions of this paragraph 6.3 apply, then:

- (a) where the User's Emergency Curtailment Adjustment Clearing Value is positive, Transco NTS will pay the User an amount equal to the User's Emergency Curtailment Adjustment Clearing Value; and
- (b) where the User's Emergency Curtailment Adjustment Clearing Value is negative, the User will pay Transco NTS an amount equal to the User's Emergency Curtailment Adjustment Clearing Value.

6.3.2 For the purposes of this paragraph 6.3:

- (a) in respect of each Day, a User's "**Emergency Curtailment Adjustment Quantity**" is the amount by which the User's Emergency Curtailment Quantity advised by the claims reviewer (or, following a referral by either Transco NTS or the claimant pursuant to paragraph 6.2.7(e), determined by the Authority) differs from the User's Emergency Curtailment Quantity estimated by the Transporters;
- (b) "**Emergency Curtailment Adjustment Clearing Value**" is an amount equal to the User's Emergency Curtailment Reconciliation Quantity multiplied by the Emergency Curtailment Adjustment Clearing Charge; and
- (c) "**Emergency Curtailment Adjustment Clearing Charge**" is an amount equal to the Daily Imbalance Charge paid by or to the User in respect of the Day to which the Emergency Curtailment Adjustment Quantity relates less the Emergency Curtailment Trade Price applicable to such Day.

6.3.3 A User's Emergency Curtailment Adjustment Quantity is negative where the User's Emergency Curtailment Quantity advised by the claims reviewer (or determined by the Authority) is greater than the User's Emergency Curtailment Quantity established by the Transporters in accordance with this paragraph 6, and is positive where the User's Emergency Curtailment Quantity established by the Transporters in accordance with this paragraph 6 is greater than the User's Emergency Curtailment Quantity advised by the claims reviewer (or determined by the Authority)."

UNC – OAD Section C

Insert the following as new paragraphs 2.7.5 and 2.7.6:

"2.7.5 In the event of Emergency Curtailment occurring in respect of a Day, each DNO shall provide Transco NTS as soon as reasonably practicable with the DNO's best estimate of the aggregate quantity of gas (in kWh) that each User would have offtaken during that

Day from each LDZ at System Exit Points in respect of which Emergency Curtailment has occurred but for the fact that Emergency Curtailment had occurred at those System Exit Points.

2.6.7 In the event that further Emergency Curtailment is required in respect of a Day, or Emergency Curtailment that had previously occurred in respect of that Day is removed, then the relevant DNO shall provide Transco NTS as soon as reasonably practicable with the DNO's best revised estimate of the aggregate quantity of gas (in kWh) that each User would have offtaken in that Day from each LDZ at System Exit Points in respect of which Emergency Curtailment has occurred but for the fact that Emergency Curtailment had occurred at those System Exit Points."

Proposed Implementation Timetable

Sent to Ofgem requesting Urgency	09/08/2005
Ofgem grant Urgent status	09/08/2005
Urgent Modification Proposal issued for consultation	09/08/2005
Closeout for representations (9 business day consultation)	22/08/2005
FMR issued by Joint Office (+4 business days)	26/08/2005
Panel approve that response reflected appropriately	31/08/2005
Modification Panel Recommendation	02/09/2005
Ofgem decision expected	07/09/2005

Code Concerned, sections and paragraphs

UNC – TPD Sections F and Q
UNC – OAD Section C

Proposer's Representative

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Proposer

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Signature