

Julian Majdanski
Network Code Development
Transco
31, Homer Road
Solihull
B91 3LT

Direct Dial: 0171-932-1674

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by post and fax 0121 711 1451

Dear Julian,

Modification 294 - Change to cash-out following an emergency

The Office of Gas and Electricity Markets (OFGEM) has today decided to reject this proposed modification to Transco's network code. Our reasons for doing so are detailed in this letter.

Currently, during a Network Gas Supply Emergency, out-of-balance shippers are cashed out at a thirty-day average of System Average Price (SAP). As part of modification 174 - Review of NDM Reconciliation Process - the following attributes were identified as desirable for a cash-out price during an emergency:

- Transparent calculation mechanism
- Easily obtainable
- Limited volatility
- Provide economic incentive to bring gas ashore (and imports from the European Interconnector)
- High enough to restrict number of claims relating to gas purchase costs
- Restrict financial exposure to under delivery

The report for modification 294 quoted these attributes and suggested that a figure of two times the 30-day SAP would fulfil these requirements.

The methodology and reasoning behind a multiple of two times the thirty-day SAP is not included in this report. To that end, Ofgem requested that Transco write to the community to seek further justification for the proposed multiplier. The responses have been limited.

The report for modification 294 also suggested that a consensus on the multiple of two times the thirty-day SAP had been reached at the Planning and Security Workstream. This would appear to be in some doubt.

Using the two times thirty-day SAP figure appears to be arbitrary and may in fact be inappropriately high. For these reasons, Ofgem has not approved implementation of this proposal. However, there do remain concerns about the appropriateness of the current cash-out price in an emergency. It may be appropriate for the industry to continue considering the issue. However, any resulting proposal would have to be better related to costs.

Please circulate this letter to all interested parties.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Amrik Bal', with a small flourish at the end.

Amrik Bal
Manager, Network Operations