

## **DN Sales Development & Implementation Steering Group Minutes**

### **Meeting 3**

17 February 2004, 9:00 am – 2:00 pm

Regus Offices, 12 St James' Square, London SW1

#### **Attendees**

Barry Watkinson	HSE	John Smith	Burges Salmon
Sebastian Eyre	Energywatch	David Ashbourne	Ofgem
Tory Hunter	Scottish & Southern Energy	Mark Feather	Ofgem
Simon Goldring	British Gas Trading	Jason Mann	PA Consulting
Keith Harris	Wessex Water	Paul Whittaker	National Grid Transco
Eddie Proffitt	MEUC	Chris Train	National Grid Transco
Nigel Nash	Ofgem	Mike Ashworth	National Grid Transco
Roger Morgan	Ofgem	Nigel Sisman	National Grid Transco
Kyran Hanks	Ofgem (chair)	Nick Wye	Waters Wye Associates
Farook Khan	Ofgem	John Costa	EDF Energy
Sonia Brown	Ofgem	Christiane Sykes	Powergen
Jess Hunt	Ofgem	Mike Pearce	Inexus representing AIGT

#### **1) Impact of Ofgem restructuring on DN sales project**

Kyran Hanks informed the group that Ofgem had recently announced an internal restructuring. As a result, Ofgem will now have a networks division and a markets division, with the DN sales project being managed by the networks division (which is headed by David Gray). One effect of the restructuring is that Kyran Hanks will become the Director of Wholesale Markets and Sonia Brown will manage DN sales in her new role as Director of Transportation.

In response to questions from the group, Kyran indicated that apart from the changes previously described, Ofgem staff involved in the DN sales project would not change and that the resources allocated to the project would not change this financial year.

#### **2) Review of minutes from previous meeting held on 3 February 2004**

The group had no additions or changes to make to the minutes.

### **3) Reports back from workgroups**

#### **a) Commercial Interface Working Group**

No CIWG meeting has been held since the previous DISG. Mark Feather said that a CIWG meeting would be held on 18 February 2004 and that the working assumptions model would be discussed.

#### **b) Agent Working Group**

Roger Morgan said that the AWG has been working to clarify the role of the agent and that this was now becoming clear. The next task of the AWG is to identify the risks and opportunities associated with the model, and then consider what mitigating action can be taken to minimise the risks. Roger also said that AWG members have expressed concerns regarding the potential costs associated with divergence and the potential for a decline in the standards of service provided to shippers.

#### **c) Regulatory Architecture Working Group**

No RAWG meeting has been held since the previous DISG. Farook Khan said that a RAWG meeting would be held on that afternoon and that the working assumptions model and the allocation of licence conditions between transmission and distribution functions would be discussed.

### **4) Actions from previous meeting**

The group reviewed the actions from the previous meeting. Each action was closed. Jess Hunt updated the group on changes to the issues log since the previous meeting.

### **5) Roles and responsibilities of DNOs**

Mark Feather gave a presentation on the role and responsibilities of distribution network owners. The options set out in the presentation included the model circulated to the group by Scottish and Southern Energy (SSE).

Tory Hunter indicated that model was not SSE's preferred option, rather it was a compromise solution that takes into account Ofgem's preference that responsibility for investment planning and contracting for interruption remain together.

A number of key issues arose during the group's discussion of Mark's presentation.

#### *Role of the DN*

Chris Train and Paul Whittaker indicated that there are critical linkages between investment planning and system operation. The system operator needs to understand exactly what was in the minds of the long term planners when they made their investment decisions. Similarly, investment planners need to understand the day to day

characteristics of the network. Consequently, NGT has proposed a model (Option 1) whereby these functions will be performed by the transmission operator on the NTS and by the distribution operator on the DN.

Tory Hunter said that SSE was not convinced that the roles of energy balancing and physical system balancing were so easily divorced as suggested under Option 1 given that Transco can call interruptions for energy balancing purposes and interruption can be called on the DN for NTS purposes. Tory argued that a single system operator would be likely to make more efficient decisions than multiple SOs. Tory also suggested that there would be a loss of economies of scale if DNs were required to establish separate system control centres. Consequently, SSE has proposed a model whereby control of investment decisions sits with the network owner but responsibility for both energy balancing and physical system balancing lies with a single GB SO.

Simon Goldring suggested the contractual relationship would be best defined when one party was SO, and that it was not possible to create a black and white split between the NTS and DN SO functions. Paul Whittaker responded that the relationship between the NTS and the DN could be expressed in numerical terms and that this relationship would be set out in the Oftake Code.

Keith Harris said that it was important to ensure that liability for network failure was clearly defined. Chris Train said that the Oftake Code set out a number of parameters and that after the next price control review these parameters would be subject to pricing arrangements and appropriate incentives.

Sebastian Eyre asked whether transaction costs associated with the NTS/DN interface could be expected to decline as a result of the DN sales process. Paul Whittaker indicated that any additional transaction costs were small compared with the potential savings associated with independent DN ownership.

The group rejected the passive DN model (Option 2) because it did not provide sufficient scope for the benefits of comparative competition to arise. Tory Hunter indicated that since Option 2 allowed the NTS to determine the level of investment on the DNs it was unattractive to potential buyers and consequently SSE did not support it. Some group members suggested that the passive DN model would be likely to find favour with financial buyers but not with buyers who wanted to run their own network.

Group members questioned how accountabilities for failure to invest and for efficient system operation would be addressed under Option 3 where the planning and operational roles are split.

**ACTION:** NGT and SSE to collaborate to provide more detail on how the relationship at the NTS/DN interface would operate under the hybrid model (Option 3) and to present findings at DISG 4. In particular, NGT & SSE were asked to explore how accountabilities for system operation and network planning would be managed under Option 3.

#### *Contractual framework*

The group rejected the third contractual model (which involves a uniform network code and short form network codes but with governance provisions that restrict the opportunities for change). The group considered that in practice, it would not be

possible to draft the restriction effectively and the result would be the same as either option 1 (UNC plus short form network codes) or option 2 (UNC).

Simon Goldring commented that innovation could be achieved under a model where there is only one network code (option 2). He also indicated that the nature of the contractual interface with shippers is a critical issue for British Gas Trading.

Some members of the group considered that the issue of whether to adopt model 1, which promotes innovation/divergence, or option 2, which promotes consistency, is a policy question for Ofgem.

**ACTION:** Ofgem to form a view on the contractual arrangements and to express view as soon as possible.

**ACTION:** Jess Hunt to circulate slides and publish on Ofgem's website.

## **6) NGT presentations**

Chris Train described NGT's position on metering, connections and IGTs and the role of SOMSAs, which is set out in papers circulated by NGT prior to the meeting and published on Ofgem's website.

In describing the SOMSA arrangements Chris Train indicated that, depending on discussions with individual network buyers, it may be possible to terminate the arrangements prior to 2006 or extend them beyond this date.

In relation to connections and IGTs, Chris indicated that a key issue is to ensure that new DN owners do not act to frustrate the development of competition in connections.

In relation to metering, Chris indicated that Transco does not intend to include its metering assets in the sale process, primarily because it does not wish to link the sales process to RGMA. The key metering issue that arises in the context of the DN sale is standard licence condition 8, which relates to the provision of meters. Ofgem is considering a proposal whereby DNs assume the responsibilities associated with condition 8, subject to an amendment such that DNs need only procure the service (rather than provide the service).

**ACTION:** Ofgem DN sales team to liaise with metering team to ensure that issues associated with metering are addressed.

## **Next meeting**

The next meeting of DISG is scheduled for Tuesday 24 February, at Ofgem's offices.