

DN Sales Development & Implementation Steering Group Minutes

Meeting 9

4 May 2004, 9:00 am – 2:00 pm

Ofgem's office, 9 Millbank

Attendees

David Ashbourne	Ofgem	Simon Goldring	British Gas Trading
Farook Khan	Ofgem	Martin Kinoulty	United Utilities
Sonia Brown	Ofgem (chair)	Paul Whittaker	National Grid Transco
Jess Hunt	Ofgem	Mike Ashworth	National Grid Transco
Jason Mann	PA Consulting	Nigel Sisman	National Grid Transco
Tory Hunter	Scottish & Southern Energy	Chris Train	National Grid Transco
Eddie Proffitt	MEUC	Sue Higgins	National Grid Transco
Keith Harris	Wessex Water	Mark Sutton	National Grid Transco
Peter Bolitho	Powergen	Nick Wye	Waters Wye Associates

Apologies

Charles Ruffell sent his apologies.

1. Review of items from previous DISG meeting held 20 April 2004

a) Review of minutes

There were no comments on the minutes.

b) Review of actions

The actions arising at the previous meeting had been discharged as follows:

ACTION: *Group members to consider the issues raised in the agency & governance and roles & responsibilities RIAs. The agency & governance RIA was due to be discussed at the meeting.*

ACTION: *Transco to provide more information about the ancillary services provided under the SOMSA. Transco's paper on ancillary and miscellaneous services under the SOMSA was tabled at the meeting.*

ACTION: *Group to provide comments, if any, on Transco's paper regarding non-discrimination provisions under Transco's licence. Transco to identify the flow-on effects that the retention of a single legal entity would have on other areas of the regulatory framework. Ofgem had not received any comments on Transco's paper. It was agreed that Transco would produce a paper on the flow-on effects of legal separation for the next DISG.*

ACTION: *Ofgem to circulate revised issues log. This action had been discharged.*

2. Report from CIWG

Sonia Brown said that the previous CIWG meeting had discussed an Ofgem presentation on issues associated with the offtake arrangements. Sonia noted that some group members believed that offtake rights should be priced. In response to a question from Tory Hunter, Sonia said that Ofgem was still considering whether pricing arrangements entailed a reopening of the price control and that this issue would be addressed in the RIA.

Sonia said that the CIWG had also discussed an Ofgem presentation that compared the options for exit reform. As a result of the feedback from CIWG members, Ofgem had added to its RIA an additional option for exit reform (Option 2C – the matrix only approach) and had also added a number of key issues for consideration.

3. Transco's proposals for UNC modification rules and governance

Chris Train summarised the Transco paper on UNC governance. He said that Transco's initial proposal is that the transmission operator runs the UNC modification process. (This approach is part of Transco's Option A model which is described in the Agency & Governance RIA.) However, the DISG paper tabled acknowledges that an alternative approach could be adopted whereby gas transporters share collective ownership and responsibility for the UNC and the modification process. In this case, gas transporters would agree jointly to create an organisation with the express purpose of managing the administrative functions of the UNC.

Peter Bolitho suggested that in a divested industry, an approach that is more inclusive of all stakeholders affected by the UNC is required. He noted that the Energy Bill will confer a right of appeal on parties that make recommendations on modification decisions. Chris Train said that it is also necessary to ensure that there is accountability for governance. He suggested that it could be possible to address some of the perceived deficiencies associated with current regime without removing accountability for governance away from the GTs. He suggested that it was appropriate for GTs to retain accountability for governance because they have the necessary expertise and a strong interest in ensuring that the UNC is effective. Sonia Brown noted that in the electricity, National Grid is able to provide its expertise in relation to BSC modification decisions without actually running the modification process. She said this arrangement facilitates debate without precluding independence.

Peter Bolitho suggested that in designing the UNC governance arrangements it was appropriate to draw on the positive lessons from other industries (although he does not advocate the adoption in full of the electricity model). He said that shippers' key concerns with the existing UNC governance arrangements are:

- ◆ the limited role of the modifications panel
- ◆ the ability of Transco to veto proposals (Chris Train noted that the veto had never been exercised)
- ◆ the lack of scope for shippers to propose alternative modifications if an amendment is required and
- ◆ the absence of minimum and maximum time limits associated with the modification process.

In relation to the final point, Peter noted that whilst general boundaries are helpful, he considered Elexon's process to be too prescriptive. Tory Hunter added that the implementation of approved modification decisions was also important. Sonia Brown noted that it appeared the group favoured a flexible timetable that can't be manipulated by any party.

Tory Hunter suggested that the modification rules themselves should be considered separately from the party responsible for managing the modification process. She said that the issues raised by Peter could be addressed via changes to the modification rules without necessarily changing responsibility.

Chris Train said that Transco would agree to more clarity and openness in the modifications process, including broader representation and the removal of the Transco veto, however, the importance of deliverability and accountability should not be underestimated.

Peter Bolitho said that it was important that shippers are involved in the governance of changes to UK Link. He favoured the development of a regulatory framework that has the potential to be amended to incorporate a wider range of stakeholders at some future date. Sonia Brown agreed that options need to be retained throughout the process, and encouraged group members to alert Ofgem if they considered that an option was being discarded.

The group discussed the extent to which the governance entity should be operated separately from the rest of the GTs' businesses. Mike Ashworth suggested that modifications would be implemented more effectively if the governance entity's secretariat understands the issues rather than simply managing the modifications process. He suggested that there was a risk of a lack of expertise and quality staff within the governance entity if strict ring fencing rules were enforced.

It was confirmed that the governance entity is intended to be a separate entity to xoserve, in order to ensure impartiality. Keith Harris questioned whether there was a role for the regulator in managing the modification process. Sonia Brown said that in accordance with the principle of light handed regulation Ofgem believed that industry should manage its own modifications process. Peter Bolitho suggested that industry should be able to make decisions itself in some instances, for instance, there may be some instances under the SPAA where no regulatory involvement is required.

Tory Hunter asked: How do the SPAA processes mesh together with other governance processes? Chris Train said that in the short term, it is possible for the UNC and SPA functions both sit within the UNC, however this is not a perfect harmony. He suggested that the SPAA could evolve so that SPA functions are removed from the UNC as more responsibility devolves to shippers.

It was agreed that the next DISG should consider the shippers' response to Transco's paper on UNC governance.

ACTION: Shippers to respond to Transco's paper on UNC governance at DISG 10.

4. Preliminary feedback on the agency and governance RIA

Sonia Brown asked the group to provide feedback on the agency and governance RIA, in particular whether there were any important issues that should be considered by the workgroups.

Tory Hunter requested further discussion of Option E. Sonia Brown said that Option E was one of a number of options developed by Ofgem in response to concerns expressed by shippers:

- ◆ Option C, where both RGTA & AT Link reside with the agency. Ofgem's concern with this option is that key operational information resides with the agency rather than Transco.
- ◆ Option D, where new systems are developed to separate settlement and operational functions. Ofgem's concern with this option is that it is potentially very costly.
- ◆ Option E where RGTA resides with the NTS, and AT Link resides with the agency. This is a compromise solution which was proposed as a result of shippers' concerns regarding the development of AT link.

Chris Train said that Transco's concern with Option E is that Transco's new system, Gemini, combines elements of both AT Link and RGTA.

Sonia Brown noted that shippers say that the majority of AT Link functions relate to settlement and Transco says that the majority of AT Link functions relate to operations. In her view, the division of AT Link functions between settlement and operations appears to be about 50:50, which makes it very difficult to decide where it should reside within the new framework.

The group discussed the implications of having one organisation or another 'controlling' a particular IT system. Sonia Brown said that under Option E, the people that use the software would be retained by the NTS, however, the people that maintain and update system would reside with the agency. She said that the key issue was data quality and a question arises as to who carries the risk associated with data quality deterioration. Peter Bolitho noted that a deterioration in the quality of NDM forecasts would have major implications for shippers.

Tory Hunter requested more clarity regarding DN information flows such as the flow of information to DNs from AT Link. In particular, she considered that DNs need to understand what information is going through the area control centres (ACCs). Chris Train said that DNs receive profiles from the NTS in accordance with pre-existing arrangements. Mark Sutton noted that most operational information flows from the DNs to the NTS.

ACTION: Transco to provide (to DISG 10) further information regarding the operational information flows received by DNs, including:

- ◆ What information is currently received by DNs? In particular, what information is received via the ACCs?
- ◆ What are the timescales associated with this information?
- ◆ How will these information flows change going forward?

- ◆ What information does the DN currently provide to the NTS?

Nick Wye raised an additional informational issue regarding credit. He suggested that IDNs could be at greater risk of default than Transco businesses because the consequences of defaulting to Transco were considerably more severe than defaulting on an IDN.

ACTION: Transco to report on how to resolve the issue of credit risk on IDNs at DISG 10.

Peter Bolitho suggested that Figure 9 in the Agency & Governance RIA should be rebased against Option A rather than the 'no agency' option, so that the differences between shippers' reported costs could be seen more clearly.

ACTION: Ofgem to rebase Figure 9 in the Agency & Governance RIA against Option A. Due DISG 10.

ACTION: Group to consider Transco's paper and presentation on the governance of the agency at DISG 10. Group members to raise any issues with Transco prior to the meeting.

5. Commercial and regulatory arrangements at the NTS-DN interface

Jason Mann gave a presentation setting out Ofgem's initial views on the key issues associated with the offtake arrangements. He said that Ofgem would like to hear participant's views regarding Transco's proposals.

Maximum Daily Quantity (MDQ) determination

Sonia Brown noted that some CIWG members had formed the view that if MDQs are determined via a planning process, then regulatory oversight is essential. She noted that pricing arrangements could be used to reduce regulatory involvement. Tory Hunter considered that pricing MDQs is an overly heavy handed approach. She suggested that it would be in GT's interests to invest efficiently since efficient investments would be allowed under the price control. Sonia responded that Ofgem's concern was that the NTS would have to bear the risk of inefficient investment because a DN demands an efficiently large MDQ.

Eddie Proffitt noted that the DN would need to determine its MDQ requirements 5 years in advance, and once the decision to build had been made, then the pipe would be in the ground for 50 years. He considered that the long term nature of these decisions meant that there was no commercial solution for investment decisions.

Peter Bolitho suggested that an administered pricing arrangement could be based on existing LRMC processes. At one extreme, the NTS could charge DN rather than shippers. Nick Wye noted that it was difficult to envisage how the NTS could allocate the costs associated with an upgrade between offtakes since multiple DNs may benefit from an investment. Nick also noted that there was a strong interrelationship between the allocation of offtake rights and exit.

Interrelationship between offtake code and NEXAs

Jason Mann said that the CIWG considered that there might be potential for discrimination as a result of differences in treatment between NEXA offtakes and offtake

code offtakes, however some members of the group felt that it was inappropriate to seek to amend the NEXA agreements. Nick Wye suggested that although it was not possible to apply charges for deviations from agreed operational flow rates under the NEXAs, it might be possible to achieve a similar result via the UNC.

Diurnal storage

Jason Mann said that some CIWG members suggested that there was potential for discrimination under Transco's proposals for diurnal storage and that the arrangements should be priced. Paul Whittaker noted that since DNs should trade-off between using NTS diurnal storage and other forms of constraint management, the case for pricing is relatively clear. Eddie Proffitt noted that questions had been raised in the CIWG as to how to value linepack.

ACTION: Ofgem to present options for allocating offtake rights to the CIWG and then report back at DISG 10 with CIWG members' views for guidance and/or directions.

6. Options for exit reform

Jason Mann gave a presentation on options for exit reform, which had been presented to the previous week's CIWG. Following the CIWG, Ofgem has incorporated a new option to its RIA (Option 2C) which is a matrix only approach. The group discussed how Option 2C would operate in practice, in particular, how network operators would receive long term signals under Option 2C.

Eddie Proffitt suggested that Ofgem was incorrect to rate the status quo negatively in relation to 'investment signals to network operators' because Transco currently receives investment signals via the 15 day + incentive. Jason Mann agreed, but noted that the signal was not as strong as under the other options. Chris Train said that there are investment signals associated with each option, but that the issue is whether the signals were efficient.

Simon Goldring noted that a question had been raised at the previous CIWG regarding the EC Directive. Sonia Brown said that this matter would be considered in the Exit RIA.

Sonia Brown said that Ofgem did not intend to discuss the exit regime at the DISG again, except insofar as was necessary to ensure that the proposed exit regime can work in the context of the offtake arrangements. She encouraged group members to raise any concerns with Ofgem.

Next meeting

The next meeting was scheduled for **10:00**, 18 May 2004.