

Development and Implementation Steering Group Minutes

Meeting 20

21 September, 10:00 am – 2:00 pm

Ofgem's office, 9 Millbank

Attendees

Julian Bagwell	Macquarie	John Dale	GTC
Rekha Patel	Conoco Phillips	Julie Cox	AEP
Charles Ruffell	RWE npower	Alan Raper	NGT
Tory Hunter	SSE	Peter Bingham	NGT
John Costa	EDF Energy	Nigel Sisman	NGT
Martin Kinoulty	United Utilities	Sue Higgins	NGT
Simon Goldring	British Gas Trading	David Ashbourne	Ofgem
Nick Wye	WWA	Farook Khan	Ofgem
Richard Street	Statoil UK	Sonia Brown	Ofgem (chair)
Peter Bolitho	E.ON UK	Jess Hunt	Ofgem
Duncan Jack	Elxon	Jason Mann	PA Consulting

1. Review of items from previous DISG meeting (held 14 September 2004)

a) Minutes

The group suggested a number of changes to the minutes of the previous meeting's minutes, which Ofgem agreed to make. Sonia Brown said that, since the previous meetings minutes were long and had only been circulated yesterday, DISG members could provide further comments after the meeting. She asked that any comments be provided by 5pm Wednesday 21 September 2004.

Action: Final version of DISG 19 minutes to be reviewed at DISG 21.

b) Actions

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

- ◆ *Transco to update the xoserve service line document to reflect Option C and deliver an overview that highlights all changes to the service lines at DISG 23. In addition, Transco to explain how it intends to implement Option C. Action due at DISG 23.*
- ◆ *Transco prepare a road map setting out a detailed forward work plan through to implementation, including the processes relating to modifying the UNC and licences, obtaining the relevant Authority, DTI and HSE consents, the implementation of the Authority's decision on agency and relevant systems changes. The roadmap should show how issues are interlinked and how overarching changes will be carried out in practice. Action due at DISG 21.*

- ◆ *Transco to report to each DISG on the UNC workstream, and to refer to the DISG any relevant issues arising at the UNC workstream. Item has been included in new agendas.*
- ◆ *NGT to explain the additional safeguards (over and above the status quo) that will protect customer's interests under the agency governance arrangements, in particular in relation to the IT systems change process. Action due DISG 22.*
- ◆ *Transco to provide update on how agency board voting rights would be allocated under sale scenario. Action due DISG 22.*
- ◆ *DISG to consider the following standard and amended standard conditions: SC/ASC 1, 4, 4A, 4D, 4E, 6, 8, 9, 16, 20, 22, 24, 25, 30, 39, 40, SpC 19, 26, 27, 28-30, 34. Licence conditions to be incorporated into forthcoming DISG agendas.*
- ◆ *Transco to give presentation on LNG issues at DISG 20. Action to be completed at the meeting.*
- ◆ *Ofgem to consider supplier's obligations with respect to metering at NTS supply points. Ofgem is considering this issue, metering to be considered at a future DISG.*
- ◆ *Ofgem to consider the application of obligations relating to metering and meter reading services and to revert to the DISG. Ofgem is considering this issue, metering to be considered at a future DISG.*
- ◆ *DISG to consider metering issues. Metering to be considered at a future DISG.*
- ◆ *Transco to consider how to build SC 22 requirements into its proposed timetable. Action due at DISG 21.*
- ◆ *Group to consider whether there should be a Designated Registrar of Pipes. Issue to be considered at a future DISG.*
- ◆ *Group to consider the availability of data formats in relation to the offtake arrangements. Issue to be considered at a future DISG.*
- ◆ *Ofgem to consider whether business separation should be required between DN-GTs and affiliated IGTs. Action due DISG 22.*
- ◆ *DISG to review the following special licence conditions: 19, 26, 27, 28-31, 34, 37. Licence conditions to be incorporated into forthcoming DISG agendas.*
- ◆ *Ofgem to provide update regarding the proposed treatment of SpC 18. Issue to be considered at a future DISG.*
- ◆ *Group to review Transco's proposed licence drafting and provide comments. Action due at DISG 23.*
- ◆ *Ofgem to report to DISG regarding the treatment of metering revenue flows under the price control. Metering issues to be considered at a future DISG.*

2. Reports from the UNC workgroup

Sonia Brown said that it is important to ensure that the UNC workgroup and DISG work together in a coordinated way, and therefore a standing agenda item relating to the UNC work group had been introduced to the DISG agenda.

Alan Raper said that the UNC workgroup is going through the code section by section, and that each session is initiated with a document which sets out Transco's view of the

required changes. He said that the issues are captured on an issue tracking log which is currently being updated.

Alan said that there is a route for actions to be escalated to DISG, and that thus far, two issues have been escalated – (1) the need for an implementation plan and (2) supplier of last resort. Simon Goldring noted that the issue of the credit arrangements is also supposed to be escalated to the DISG from the UNC workgroup.

Action: Transco to present on credit arrangements to DISG.

Alan said that Transco intends to prepare minutes of future UNC workgroup meetings in order to ensure that continuity is maintained. Sonia welcomed this move. Alan told the group that Transco is using the network code distribution list as the mailing list for the UNC workgroup.

Peter Bolitho expressed concern about the status of the UNC workgroup in relation to the formal UNC modification procedure. Peter considered that there could potentially be an abuse of process if existing modification rules are not used. He explained that Eon UK has put forward a modification proposal which proposes the establishment of a new group that would work in parallel to the UNC workgroup. This group would operate within existing procedures as set out in the Network Code.

Transco suggested that this would result in a duplication of effort. Sonia noted that Transco has previously given a number of presentations to the DISG regarding the UNC workgroup and these concerns were not raised. She asked whether Eon UK's concerns arise as a result of the operation of the process, or because the group is in the incorrect forum. Peter said primarily the latter. He said that there is an official process for changing the Network Code and eventually a Network Code modification proposal will need to be considered. He said that the objective of the modification proposal is to ensure that proper process is followed. Peter suggested that, if proper process is not followed, any decision may be vulnerable to challenge. Eon UK's modification proposal was intended to close the process loop.

Sonia suggested that the purpose of the UNC workgroup is to carry out the preliminary work required to develop proposals for a new document. She said that the formal modification rules would be adhered to at a later stage in the process. Peter Bolitho considered that the development of the UNC is fundamentally about the demise of the Network Code, and consequently if a 'fait accompli' mod were to be presented to industry in March it could be vulnerable to challenge. Alan Raper said that it was necessary to develop the UNC outside the Network Code modification process because many of the concepts being considered in relation to the UNC, such as multi-transporter arrangements, do not exist within the current framework. He suggested that the UNC workgroup is a 'pre-consultation process'.

Peter Bolitho said that the process proposed in Eon UK's modification proposal was intended to be complementary to existing processes rather than duplicative. He said that the objective of the proposal is to ensure that the transition from the Network Code to the UNC is effective. Richard Street observed that Peter's proposal was intended to address a risk and it was not intended to disrupt the process.

Sonia Brown agreed that Network Code modification would be required to move from the current Network Code to a short form network code. She asked Transco about the process that they planned to adopt for this stage of the reform process. Alan Raper said that in moving from A to B, it was need to work out what B was before they could decide how best to get there. He said that in Transco's view, the development of changes to get to the UNC should not be part of the mod process. Rather, a modification proposal should be raised after UNC development is complete. Sonia

Brown noted that shippers are concerned that if a mod is raised at the 11th hour, then entire process may be vulnerable to challenge.

Simon Goldring added that shippers were also concerned that the sheer volume of work was being underestimated and consequently issues will be left unresolved.

Sonia Brown said that it would be helpful for Transco to develop a constructive way of moving issues forward. She said that the burden of proof is on Transco to make stakeholders comfortable about their process. Sonia noted that Transco's forward plan (the 'roadmap') was due to be discussed at DISG the following week, and asked the group if they were prepared to wait until next week to form a view on whether they are comfortable with the proposed way forward.

Rekha Patel asked for roadmap to be circulated prior to meeting. Transco agreed to this.

Action: Transco to circulate roadmap prior to DISG 21.

Peter Bolitho said that there is likely to be a postal vote in relation to Eon UK's mod proposal in 2 weeks. Simon Goldring noted that the timing of the postal vote was designed to accommodate discussion of Transco's roadmap at next week's DISG.

Alan Raper said that if Eon UK's proposal relates to transition rather than duplication then Transco would be unlikely to have a problem with it. He suggested that the proposal may need to be more tightly scoped.

John Costa asked Transco whether they had considered establishing a review group within the existing modification framework. Alan Raper said that Transco had considered this but formed the view that this approach would not work because the appropriate governance arrangements do not exist. Peter Bolitho suggested that the existing governance arrangements should apply as Transco was proposing changes to the existing code.

Sonia Brown said that Ofgem has adopted an open door policy in relation to DN sales issues. She invited participants to raise any concerns with Ofgem on a bilateral basis.

In relation to other DN sales-related workgroups, Jess Hunt noted that the next SPAWG meeting was scheduled for 4 October.

3. Transco presentation on the new licence conditions

Sue Higgins gave a presentation setting out Transco's view of the new licence conditions that could be required as a part of the DN sales reforms. The list compiled by Transco is primarily based on the issues identified in the informal licence consultation but also it also includes additional potential conditions that have arisen in subsequent discussions.

Martin Kinoulty noted the potential new condition relating to the Offtake Code, and asked whether this meant that it was confirmed that an offtake code would be established. Sonia Brown said that this position was not confirmed, and that Transco's list is intended to cover off all potential new conditions.

Martin Kinoulty asked when interested parties were likely to be able to see the proposed drafting. Sonia Brown said that the drafting would not be made available until the issues were settled, and that Ofgem is working with Transco to develop a timetable for the drafting of the conditions. She said that whilst it was important to engage the DISG in this process in order to obtain industry feedback, it would not be helpful to end up drafting by committee. She proposed that Transco will initially draft the conditions and then DISG members would have the opportunity to provide comments at the meeting.

Martin Kinoulty asked when key points were likely to be resolved. Peter Bingham said that Transco's roadmap will set out a way forward in relation to the UNC and licensing arrangements, however it would not include the offtake arrangements as Transco is awaiting a decision from the Authority in relation to the governance of the offtake arrangements. Rekha Patel expressed her disappointment that the offtake arrangements would not be included in Transco's roadmap.

Sonia Brown said that the governance of the offtake arrangements was a key decision that the Authority was currently considering. She indicated that there were a number of difficult issues arising which meant that it is not currently possible to provide a final answer, however, Ofgem is seeking to provide an answer as soon as possible.

Julian Bagwell suggested that a lot of the work can be progressed regardless of whether it finally resides in the UNC or an Offtake Code. Sue Higgins agreed that the substance of the offtake arrangements can be developed. Julian Bagwell said that it was important that the roadmap sets out all linkages or else it will be impossible to get an understanding of the workload that is required.

Sonia Brown returned to the issue of the licence conditions. She asked the group whether Transco's list was comprehensive.

Julian Bagwell noted that the requirement not to prejudice another GT's system would give rise to big liability issues, and consequently the condition needs to be drafted very carefully. Sue Higgins suggested that Transco were intending to draft a condition similar to the condition that appears in the shippers' licence.

Simon Goldring said that it was important that the concept of the overall system is not lost. He suggested that end consumers don't want to lose the single consistent system. Sonia Brown asked how this could be achieved. She asked if this entailed hardwiring the Authority's decision on roles and responsibilities into the licence. Simon said that it was necessary to recognise the different operational arrangements (although he was not convinced that hard-wiring is the correct solution) however, it was also important to make sure that the future development of GB system occurs in a coordinated manner. Sonia said that she was not sure how Ofgem could impose an obligation on GTs to consider the whole network if it doesn't relate to what the DN is doing.

Simon Goldring asked whether it would be possible, under the proposed licence structure, to end up with a fourth category of licence conditions - Amended Special Standard Conditions. Sonia said that this was legally possible however it would be contrary to the policy intent of the proposed structure. She suggested that, in practice, Ofgem would seek to make such conditions a Special Condition. Farook Khan noted that a Standard Special that was amended through private CLM process would remain a Standard Special.

Again, Sonia Brown emphasised that Ofgem wants to understand everyone's perspectives on these issues, and that the opportunity to raise issues bilaterally is there for everyone.

4. Transco paper on treatment of DN entry points

Nigel Sisman explained that there are two DN entry points where gas is taken into the system: Hatfield Moor and Wytch Farm. He said that these entry points are defined in the licence and that the gas flows associated with these input points are very small. These DN entry points are treated in the same way as commercial entry points admitting gas directly into the NTS, including in relation to capacity allocation & the treatment of gas inputted. Nigel said that capacity can be bought through auctions, however, as far

as he is aware, there have been no requests for either long term system entry capacity or for capacity above baseline. Any applications for LTSEC above baseline would be considered in a similar way to all other entry points in accordance with the IECR methodology. Nigel noted that there is potential for capacity above baseline to be sold and that in this case, the NTS would be exposed to buy back risk, just as it is in respect of any other capacity release at any entry point and in respect of capacity entry capacity level sold. He said that it is up to the NTS to manage this risk with DNs.

Nigel explained Transco's proposal that the NTS continues to sell capacity at DN entry points, and if capacity above baseline is requested, then the NTS could release non-obligated capacity, but this would only occur after discussions with the DN. He said that the revenues associated with the provision of capacity at DN entry points would continue to be treated as defined in the NTS SO incentive arrangements, i.e., would continue to flow into NTS SO incentive pot. Nigel said that these revenue flows are relatively small and that the baseline capacity associated with DN entry points is approximately 4 GWh per day, however actual flows are usually a lot less. Nigel said that the overriding objective of Transco's proposed method of dealing with these entry points is to preserve the NBP.

Tory Hunter noted that under this approach, the NTS decides how much capacity is sold and gets the associated revenues, but the DN must pay if it doesn't have capacity available. Nigel Sisman confirmed that this was the proposal suggested that there is a question of materiality. He said that it is highly unlikely that the DN would need to provide additional capacity (or buy back) during the current price control because the DN entry points haven't given rise to any buy back to date.

Sonia Brown noted that Transco's proposals appeared to be quite unusual. Nigel Sisman said that he didn't think the proposal was unusual, given that this arrangement is supported by the existing NTS SO incentives. Sonia said that the price control was set on basis of a single GT and noted that Transco had not supported the re-opening the price control in the context of DN sales. Nigel confirmed that this was the basis under which Transco wished to conduct the sale and that this was transparent although the potential implications were anticipated to be immaterial.

Nick Wye and Richard Street noted that if the revenue flows were immaterial, then it appears more appropriate for the flows to pass to the IDNs. Sonia Brown said that Ofgem would need to consider the incentives on the NTS and DNs under Transco's proposals. She said it would be important to ensure that the GTs obligations are being fulfilled, both on day 1 and going forward.

Jason Mann sought confirmation from Transco that there are only two DN entry points. Transco said that Hatfield Moor and Wytch Farm were the only DN entry points, however there are also some ancillary flows at some LNG sites.

Sonia Brown asked whether the relevant pipes are sole usage.

Action: Transco to confirm whether the pipes associated with DN entry pipes are sole usage.

Tory Hunter asked whether the assets associated with the DN entry points have been sold as a part of the DN sales transaction. Nigel Sisman explained that under Transco's proposal, the assets will belong to the IDNs, however the revenue contributes to the NTS SO allowed revenues and not the DN allowed revenue stream.

Simon Goldring asked who shippers would contract with under the proposed arrangements. Nigel said that shippers would contract under the UNC in a similar

manner as now. He added that the connection agreement associated with the entry point would be with the DN but capacity would be sold by the NTS.

Nigel Sisman said that the arrangements relating to DN entry points may warrant consideration at the next price control, for instance it may be appropriate to include an allowance for DN entry points in DN allowed revenue and to remove the entry points from the NTS incentive schemes.

Julie Cox noted that whilst DN entry points might not be an important issue at the moment, there may be problems going forward. Sonia Brown agreed that it was important to make sure that the arrangements are enduringly robust.

Sonia added that it is also important to ensure that new entry points are developed in a way that is economic and efficient. Peter Bolitho suggested that in this context, it may be useful to have regard to both the positive and negative experiences of embedded generation in electricity.

Action: Transco to set up a meeting between GTs and Ofgem to discuss the treatment of DN entry points and report back to DISG.

5. Transco paper on Supplier of Last Resort (SOLR)

Alan Raper explained the background to this issue, which arose in UNC workgroup discussions. He said that Transco had been surprised by shipper's adverse reaction to Transco's proposal that the SOLR provisions would not commence unless there was a nationwide termination.

Charles Ruffell said that shippers were concerned about Transco's proposal that a DN that is defaulted upon would be able to offer the shipper's customers on a notice board, however, they would face exposure in the meantime. Martin Kinoulty noted that if a shipper is in real trouble, then there is likely to be a rolling effect, however, it is important to consider how liabilities would arise. He suggested that in practice, the issue was a credit issue not a SOLR issue. Sonia noted that, once again, the issue appeared to be related to the perception that shippers would have different incentives for default in relation to different networks.

Simon Goldring suggested that there was an issue as to whether there should be a regional SOLR as well as a national SOLR. Jess Hunt noted that Ofgem's original proposal relating to multiple SOLRs was not regional but rather that it might be appropriate for a defaulting shippers' portfolio to be allocated among more than one SOLR. Sonia Brown noted that in the electricity industry, a SOLR is not appointed in relation to a local transportation default.

Action: Transco to consider SOLR as part of its presentation on credit issues.

John Costa asked whether arrangements to ensure a smooth transition if a GT becomes financially distressed were required. Sonia Brown noted that the new Special Administrator provisions in the Gas Act deal with this issue.

6. Transco paper on securing co-operation in relation to CV shrinkage

Nigel Sisman gave a presentation setting out Transco's view on how the arrangements for CV shrinkage would operate in a post DN sales environment.

Simon Goldring asked whether, in future, each GT would have the opportunity to put forward their own methodology for the determination of CVs. Nigel Sisman said that he did not know and would respond to the group on this question.

Action: Transco to confirm whether there is scope for divergence in the CV methodologies in a post-sale sales environment.

Nigel Sisman suggested that DNs have an incentive to ensure that CV shrinkage does not occur because the application of the cap would mean that the DNs lose out on allowed revenue via the price control. Nigel also noted that the NTS also has an incentive to ensure that CV shrinkage does not exceed the cap through its shrinkage incentive arrangements. He concluded that NTS and DN interests were well aligned in this case.

Nigel said that it may be feasible for the NTS to configure its system to mitigate the loss, however this approach cannot completely address the risk. He said that the DNs also have the opportunity to affect the level of CV shrinkage, in that DNs could choose to nominate/ configure networks in a way that reduces the flow weighted average and hence the level (if any) of CV shrinkage. Nigel said that it is likely that DNs would take advantage of these opportunities. He added that in the long term, investment might be used to mitigate the level of CV shrinkage losses.

Sonia Brown noted that in the future, DNs and other NTS connectees could be required to pay for their use of system flexibility. She suggested that it would be necessary to consider the arrangements for ensuring an efficient level of CV shrinkage in the context of the new arrangements for operational flows. Richard Street noted that the NTS could potentially impose costs on the rest of the industry in order to maximise its own interests as there is an interaction between diurnal storage and CV shrinkage. Sonia Brown said that the issue should be considered in the context of the development of incentive schemes.

Nick Wye asked Nigel how frequently the cap is employed. Nigel said the events were exceptionally rare and of very low effect suggesting that in his view the losses were probably less than 1% of shrinkage (ie 1% of 1%).

Nigel explained that under Transco's proposals, DNs would reimburse the NTS for CV shrinkage costs incurred due to reasonably foreseeable circumstances associated with DN CV or volume measurement equipment. Jess Hunt asked if the reimbursement arrangements would be one sided, or if the NTS would reimburse DN for costs associated with lowering NTS CV shrinkage. Martin Kinoulty said that there should be some form of economic test to ensure that the GB system is operated in an efficient manner overall.

Nigel Sisman said that under Transco's proposal, the NTS would not be required to reimburse DNs for costs associated with lowering the level of CV shrinkage. He said that Transco's proposals (as set out in the offtake code) formed part of the sale and purchase agreements and consequently could not be renegotiated at this point. Sonia Brown said that there must be an opportunity for such aspects of the offtake arrangements to be reconsidered as the Authority has not yet consented to the transaction. She said that the price that purchasers paid for the business reflects the uncertainty regarding the regulatory arrangements.

Action: Group to keep the CV shrinkage arrangements under review in the context of the wider offtake issues.

7. Transco presentation on LNG arrangements

Sue Higgins said that the LNG arrangements arise because it is necessary to decide whether LNG licence conditions should apply to DN-GTs, NTS-GTs or both. She said that in Transco's view, the conditions should apply only to NTS-GTs as the vast majority

of flows from LNG facilities flow into NTS and only a few ancillary flows go from LNG facilities into the DNs. She noted that operationally, these ancillary flows cannot be diverted from the DNs without great expense.

John Costa asked whether DNs currently pay the NTS for the gas that is diverted onto their networks via LNG storage facilities. Sue Higgins explained that Transco LNG has NBP account and balances its position each day, and that LNG charges reflect this cost.

Sue explained the contractual framework that would accompany the LNG arrangements. She said that the agreement between the NTS and Transco LNG stay same, however it would be necessary to develop a new DN-LNG agreement to preserve operational arrangements. Sonia Brown suggested that it may be necessary to consider whether changes are required to NTS-LNG agreement to reflect the offtake arrangements. Sue Higgins indicated that in Transco's view, LNG storage is unique and consequently there should be separate arrangements applying to the LNG offtakes.

Simon Goldring asked whether LNG-DN arrangements would be commercial arrangements. Sonia Brown added that it was necessary to make sure that the DN receives its capacity allocation in accordance with the offtake arrangements. Sue Higgins suggested that the ancillary flows from the LNG facilities would offset from other flows from the NTS. Richard Street suggested that this arrangement needs to be squared off contractually.

Sue Higgins said that the flows were so small that a materiality point arises. Sonia Brown said that if these flows are immaterial, then Transco NTS needs to be aware that it is taking a risk that it may be subject to underrun charges. Sue Higgins and Peter Bingham suggested that Transco NTS would be willing to accept this risk because flows are generally inputted in summer when there is little risk of underruns being relevant.

Jess Hunt asked whether the DN-LNG agreements would consider gas quality issues, including liabilities if the gas flowing from the LNG storage facilities gives rise to a gas quality incident. Sue Higgins said that she had not seen the contract, however she was not aware that it included gas quality. She noted the GSMR requirements are met at present and therefore they should continue to be met going forward.

Simon Goldring asked why Isle of Grain was not also included in the proposed LNG arrangements given that the same issues arise. He noted that a number of the items discussed during DISG 20 relate to similar issues and Transco has put forward a different solution in each case. Sonia Brown said that Transco needs to give careful consideration as to whether their proposals are not unduly discriminatory.

8. Other business

Julie Cox asked when an updated rolling agenda would be made available to DISG member.

Action: Ofgem to circulate an updated set of forward DISG agendas.

9. Next meeting

The next meeting will be held at Ofgem's offices on 28 September 2004.