

Development and Implementation Steering Group Minutes

Meeting 22

19 October, 10:00 am – 2:00 pm

Ofgem's office, 9 Millbank

Attendees

Sonia Brown	Ofgem (chair)	Sharif Islam	Total
Jessica Hunt	Ofgem	Lisa Waters	Macquarie
Jason Mann	PA Consulting	Julian Bagwell	Macquarie
Farook Khan	Ofgem	Peter Bolitho	E.ON UK
Liz Hillman	Ofgem	Martin Kinoulty	United Utilities
Matteo Guarnerio	Ofgem	Tory Hunter	SSE
Peter Bingham	NGT	Charles Ruffell	RWE Npower
Sue Higgins	NGT	Rob Cross	Statoil
Graham Barnett	NGT	Duncan Jack	Elexon
Nigel Sisman	NGT	Sebastian Eyre	energywatch
Mike Ashworth	NGT	John Costa	EDF Energy
Alan Raper	NGT	Alison Kuch	BGT
Mike Young	BGT	Julie Cox	AEP

1. Review of items from DISG 21 (held 19 October)

a) Review of minutes

Sonia Brown stated that, given the short period of time between the previous and this meeting, minutes from DISG 21 will be reviewed at DISG 23 (scheduled on 26 October).

b) Actions from previous meeting

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

- Transco to present on credit arrangements to DISG. Transco will be undertaking this action at a future DISG.
- Transco to consider SOLR as part of its presentation on credit issues. To be discussed at DISG 23.
- Transco to confirm whether there is scope for divergence in the CV methodologies in a post-sales environment. To be delivered to DISG 23.
- Ofgem to update a list of forward agendas. Ofgem will try its best to deliver this as soon as possible.
- Transco to review the timetable process that has been set out after the launch of the 8AA consultation. Discussed at today's DISG.

- Transco to expand the safety case section of the route map to highlight all of the roles of the HSE and DTI. Discussed at today's DISG
- Transco to include the delay to the safety case submission and the processes to be followed after hive down on the road map. Discussed at today's DISG.
- Transco to deliver its view regarding how the process of transition from the Network Code to the UNC will work. To be discussed at DISG 23
- Transco to update DN operators regarding the changes to the systems that will be required to support a 2A world. Outstanding. Transco agreed to update potential buyers on this issue.
- Transco to report back to DISG 22 regarding IDNs position in relation to the extension of emergency services contracts for IGTs. Graham Barnett noted that all emergency services contracts with IGTs have been extended to 2006.
- Transco to clarify how the emergency procedures will work in practice, particularly in relation to local emergencies. Transco agreed to discuss this issue at the UNC workgroups and to escalate it to DISG only if a solution could not be found there

2. Amended roadmap (Transco)

An amended version of the roadmap was distributed to the group. Sue Higgins explained the new roadmap that sets out the proposed timetable for developing and implementing changes to:

- Licences;
- DTI exemptions;
- Safety Case;
- industry agreements;
- transition approach (dealing with new and existing mods, system changes, invoicing and billing queries);
- changes to the network code to create a SFC;
- xoserve;
- Joint Office;
- industry seminars; and
- implementation planning (including credit arrangements processes).

Tory Hunter noted that the timetable for approval of safety case v5 is far more restricted than that for v4. Mike Ashworth explained that this is because the last change essentially involves only a name change. Sonia Brown noted that the proposed timetable for this issue has not changed from previous timetables. Sonia also noted that this is an indicative timetable and it does not make assumptions on the decision on whether the offtake arrangements should be included within the UNC.

Julian Bagwell asked whether HSE have agreed to have one month to reach a decision on iDN Safety case v5. Mike Ashworth replied that they have agreed to try to work within that timeframe.

Charles Ruffell asked whether the DTI agreed to consult on an exemption. Sonia Brown replied that the DTI are getting policy clearance within Whitehall, and are asking whether there is any objection on them consulting on these issues.

Sonia, asked by Julie Cox, explained that the scope of the exemption is to deal with the NTS-DN interface and will not cover NTS direct connects. She noted that under the

proposed arrangements shippers will be responsible to book capacity on behalf of NTS direct connects.

Peter Bolitho asked what the difference between JO rules and constitution is. Sue Higgins explained that the latter is an agreement between DN-GTs which constitutes the JO (dealing with funding, etc.), while the former are broader rules on how the JO will work and include the role of the subject matter experts (SMEs).

Graham Barnett asked for comments on the agency services agreement so that Transco will be able to feed them back to the next SPAWG.

Action: DISG members to provide Transco with comments on agency services agreements by mid November. Transco to consider these comments when preparing an updated paper for discussion at December SPAWG.

Martin Kinoulty asked when Ofgem will be publishing a consultation document on incentive arrangements.

Action: Ofgem to update DISG members on the status of the consultation document on incentive arrangements.

Sonia, asked by Lisa Waters, clarified that, as regards industry arrangements, "sign off" of legal drafting on Transco's amended roadmap refers to discussion by DISG. Sonia suggested that the roadmap could be clarified. Lisa Waters also asked whether additional mods are required to facilitate the transition. Mike Ashworth replied that the majority of transitional rules would be part of the closing modification proposal.

Peter Bolitho stated that it would be logical for transition arrangements to be included in the current Network Code in order to create a clear break between the periods before and after DN sales.

Sonia Brown noted that this issue is covered within the amended roadmap either under the UNC work strand or the network code work strand.

Nigel Sisman asked what the transitional arrangements will cover. Peter Bolitho said that they would cover issues such as settlement/billing processes relating to transactions prior to DN sales and he reiterated that a clear break between pre and post DN sales can be advantageous.

Action: Transco to report to DISG 23 on the contractual basis of transitional arrangements

Tory Hunter noted that the HSE decision is set to be before the 8AA decision. Sonia noted that clearly there is a risk element if some modifications were considered to be key by the HSE.

Asked by Charles Ruffell, Sonia noted that there will be a separate work strand led by Transco on exit arrangements.

Julian Bagwell said that it would be helpful if interdependencies between the different work strands are shown on the roadmap. Sonia agreed that a separate roadmap showing interdependencies should be prepared by Transco.

Action: Transco to provide two versions two versions of the roadmap, a “clean” one and one which shows interdependencies.

3. Transition from Network Code to Uniform Network Code (Transco)

Peter Bolitho distributed copies of an email sent to Ofgem in which he expressed his concerns about the method of transition from the Network Code to the UNC. In this email, Peter had outlined the following issues:

- Will the Network Code become the short-form code for Transco (RDNs or NTS, both)?
- Would not termination of the Network Code and designation of completely new codes be better?
- In what document should the transition and run-off arrangements sit?
- How do we ensure all transportation arrangements (NTS and DNs) are subject to the UNC modification rules and no other change procedures?

In response to these concerns, Alan Raper gave a presentation on the UNC development process. Alan outlined the proposed contract model and described the process envisaged in order to create the UNC and the short-form codes. Finally he explained the signing requirements for shippers.

Alan, asked by Julian Bagwell, confirmed that under the proposed approach the framework agreements will need to be signed before hive-down, during the period between 18 April and 1 May 2005.

In response to a question from Peter Bolitho (first point in the email), Sonia said that the form that the short form code will take is linked to wider considerations that Ofgem is giving to legal separation. Sonia said that the Authority decision on legal separation is a “minded to” decision and Ofgem needs to do further work with Transco on this issue. Mike Ashworth noted that substantive rules will not appear in the Short Form code. Rob Cross asked whether other documents that are currently linked to the network code will be included within the UNC. Mike Ashworth said that the issue was unlikely to prove problematic, since references to Transco’s network code can be passed over to the UNC. Tory Hunter asked how Transco’s Network Code will continue to exist if it is modified into a short form code. Mike explained that Transco’s short form code is a continuation of the current network code.

Peter Bolitho reiterated his point that it seems strange to have a document that relates to the situation prior to DN sales continuing to exist post DN sales without a clear cut. Mike replied that the proposed approach has been designed specifically so that existing arrangements can continue and a situation where these arrangements are cancelled on hive down is avoided. Sonia noted that since the early stages of the work on DN sales (including the July 2003 consultation document) continuity of arrangements has been seen as a gateway requirement by Ofgem, especially with respect to gas balancing. Peter Bolitho did not disagree with the principle of continuity, but he noted that there was a clean break in the case of BETTA. Alan Raper replied that, in practice, the termination of the network code cannot be a clean break.

Peter Bolitho said that the run off arrangements should stay within the current network code. Sonia Brown asked him why, as long as shippers obtain continuity between the network code and the UNC, he considers this issue to be important. Sonia also asked

what the risk associated with placing the run off arrangements within the UNC would be. Peter replied that he is suspicious as to why these arrangements are addressed in such a complicated way. Mike Ashworth noted that the final modification proposal will strip down the network code and place it within the UNC and, as a matter of contract, the same contract will remain in place. Mike Ashworth, asked by Sonia, also stated that there will be a separate transitional section in the UNC and it will be clear that Transco, not IDNs, has obligations in relation to the previous arrangements.

Sonia noted that a diagram showing a mapping of different obligations into the licence would be helpful. Alison Kuch suggested that it would be useful to see some scenarios of possible disputes with shippers in the transition. Sonia invited shippers to prepare some scenarios of situations which may create concerns.

Action: Shippers to prepare scenarios of possible disputes due to transition between NC and UNC. Transco to report on the scenarios presented. This needs to be discussed at the UNC Development Forum, and, if not resolved, escalated back to DISG by DISG 26.

DISG members confirmed that they accept the high level framework on transition presented, therefore Sonia suggested that this issue needs to come back to DISG only if detailed issues arise that cannot be resolved in workgroups.

4. Private CLM (Ofgem)

Jess Hunt gave a presentation on the proposed “private” collective licence modification procedure.

Jess noted that in the absence of new private CLM provisions, Ofgem would require the consent of an individual licensee to uniformly change the majority of the NTS and DN GT licence conditions. Therefore, the licensing framework would become unwieldy and costly to administer and there would be a risk that the NTS and DN licences could diverge and become inconsistent, an outcome that could potentially be detrimental to the interests of consumers. Jess explained that the private CLM mechanism, which is required because the Gas Act does not cater for separate NTS and DN GTs, resolves this issue.

Jess described the structure of the proposed condition, and she explained that relevant licence holders are able to prevent the Authority from directing a modification where either of the following two tests are met:

- The objecting licence holders constitute at least 20% of relevant licence holders; or
- The objecting relevant licence holders account for at least 20% of market share

Jess then outlined the implications of using the Gas Act model, and detailed the way forward. She said that the proposed private CLM licence condition drafting has been published on Ofgem’s website and comments would be welcome by 29 October. She explained that if required by the responses, further discussion will take place at DISG 24 and further proposals will be put forward in the November licence consultation document.

Sonia Brown highlighted that the proposed approach has an important safeguard since it is necessary to require the licensee's consent in order to insert the private CLM condition. Sonia explained that the proposed approach is undertaken in order to make the process manageable, given the absence of primary legislation.

Sonia, answering a question from Alison Kuch, explained that SSE had requested two licences; therefore Ofgem intended to grant two licences for the SSE DNs but only one licence for the NGT RDNs, in accordance with the licensees' preferences. Sonia also said that the DTI has not commented directly on the licence consultation document but has been working closely with Ofgem on several aspects of DN sales.

Julian Bagwell stated that with a maximum of only nine parties, he was not convinced that the market share test is appropriate in the case of gas transporters. Sonia acknowledged this point, but she said that as far as possible Ofgem is trying to replicate the existing statutory provisions. Peter Bolitho suggested that Ofgem could avoid fragmentation of licences without a private CLM procedure by not directing licence amendments unless all licensees accept the change.

5. Amended Standard Conditions 4 & 4A (Transco)

Amended Standard Condition 4 – Charging Gas Shippers - General

Sue Higgins detailed the proposed changes to Amended Standard Condition 4 (Charging Gas Shippers – General) of Transco's GT licence under the section 8AA process. As regards the proposal to impose a reasonable endeavours obligation on the licensee not to make changes to charges more than [once] per year and to make such changes on a specified date [1 October], Sue noted that it is NGT's view that either such an obligation should not apply in respect of NTS charges or that any such obligation should allow for the changing of charges at least twice per year. Sue also described the proposed amendment to the condition, which would oblige the licensee to comply with the provisions of the joint governance arrangements relating to the administering of the coordination of charging changes. Peter Bingham said that he believed that many GTs may need to change charges more frequently than once per year. Sue Higgins noted that having an obligation to change charges once per year might create more instability than twice per year. Peter Bolitho said that it is important to have aligned charges. Sonia said that an alternative to the proposal may be to have two changes per year in a given window, possibly associated with a best endeavours obligation. Sonia welcomed views from DISG participants and interested parties on this issue.

Amended Standard Condition 4A – Obligations as regards charging methodology

Sue explained that the proposed amendments in this section to be introduced under the S8AA process are:

- Impose a reasonable endeavours obligation on the licensee not to make changes to the charging methodology more than [once] per year and to make changes on a specified date [1 October]
- Oblige the licensee to keep the charging methodology under review at all times
- Oblige the licensee to comply with the provisions of the joint governance arrangements relating to the administering of the coordination of charging methodology changes

Tory Hunter noted that the obligation to keep the charging methodology under review at all times may be unduly onerous and difficult to comply with. Sonia stated that there might be merit in reflecting the drafting of the NGC licence. Sonia agreed that the drafting of 2A(b) in ASC4A needs to be reviewed.

6. Amended Standard Condition 9 – Network Code

Sue Higgins noted that this condition has been drafted in three separate parts, namely:

- Network Code;
- Joint Governance Arrangements; and
- independent market for balancing

In addition, she presented a section detailing the interpretation of the relevant terminology.

Network Code

Tory Hunter asked whether this condition contains the agency obligations. Sue replied that potentially there could be a separate agency licence condition, although there might be some overlapping between the two conditions.

Alison Kuch noted that the provision on use of common systems would not apply following the grant of a licence under the current drafting. Sonia agreed that this aspect of the drafting required attention. She also clarified that the definition of a connected person may be different from the drafting presented depending on policy decisions.

Peter Bolitho noted that clause 3 of the proposed Standard Special Condition on Network Code may be superfluous, since he considered that the issue was covered already in clause 7. Tory Hunter replied that the two clauses refer to different issues. While clause 3 allows for divergent codes with Ofgem's consent, clause 7 relates to modification procedures. Peter expressed his concern that this might be considered as an invitation for divergent short form codes to emerge. Several members of the group replied that it is normal to include such a clause.

Peter asked for clarification on the modification procedures that will be in place if aspects of the GT-GT relationship are included in the UNC. Sonia said that it is very important to clarify which parts of the UNC relate to the different parties in order to ensure that the modification procedures reflect this. Peter stated that it is important to establish the principle that shippers have the right to modify all parts of the UNC, in order to have continuity with the previous arrangements. Sue Higgins replied that there might be areas where this would not be appropriate. Tory Hunter stated that only relevant parties should be able to modify the arrangements. Sonia said that it will be important to undertake this discussion when a decision on the offtake code is made.

Rob Cross asked for a clarification on clause 22 of the proposed Standard Special Condition. Mike Ashworth explained that parties other than shipper sometimes have the right to make modifications to the network code, and the term "shipper" includes these third parties.

Joint Governance Arrangements

Sue described the proposed wording for the part of the licence condition related to Joint Governance Arrangements.

Alison Kuch said that the proposed role of the Joint Governance Arrangements is very wide. In particular, she noted that clause 1(a)(vii) refers to “such other matters as they may decide”. Alison asked for some examples. Sue replied that she did not have examples since the proposals are still being developed. Alison suggested that a clause could be added, stating that the relevant documentation will be published (and where – e.g. website). Julian Bagwell asked whether condition 2A should include a requirement to ensure compliance with the network code rather than with modification rules only. Sonia stated that the constitution of the Joint Office is different from Elexon, and it is not within the code but in separate agreements which only parties to the agreement can change. Sonia said that there is an implied obligation on licensees to ensure compliance following changes to the code. Mike Ashworth stated that clause 1(a) is a “pseudo relevant objective”.

Action: DISG participants to provide feedback on issues/questions on the initial licence drafting.

Action: Transco to set up and manage a specific issues list for licence drafting

Independent market for balancing

Sue explained that the current assumption is that these provisions will remain relevant to the NTS licence only. She also noted that, while the relevant provisions will be contained in the UNC, they will only apply to the NTS operator.

Alison Kuch said that the gas balancing market should be independent of all GTs not just the licensee.

Tory Hunter asked what changes will be required in the S23 document. Sonia explained that Transco’s document suggests changes to the licence conditions relating to the separation of price controls. Sonia said that comments on Transco’s drafting are required urgently, and she explained that a section 23 notice will be issued in November. She noted that more structural changes will be considered at the Section 8AA stage.

7. Customer safeguards under Transco’s agency governance arrangements (Transco)

Action: Transco to present at DISG 23.

8. Xoserve voting arrangements (Transco)

Action: Transco to present at DISG 23.

9. Cash flow under the proposed Offtake arrangements (Transco)

Nigel Sisman gave a presentation detailing the cashflows under the proposed Offtake arrangements. He noted that over past weeks there had been a hold up in establishment of a policy position on the definition of the exit capacity product (in particular on the zonal/nodal issue). However he hoped that this blockage could be overcome shortly so

that detailed development could proceed. Nigel suggested that the reform proposals would not take effect until systems had been developed to support the new regime.

Nigel stated that this was the first of a series of presentations for DISG that would outline the framework that will define the basis for DN sales implementation should the appropriate consents be granted. Firstly, Nigel described the structure of NTS charges.

He said that NTS revenue is recovered through the following charges:

- NTS Entry capacity charges (levied upon entry capacity purchased – entry capacity payments are auction based)
- NTS exit capacity charges(levied upon exit capacity holdings)
- SO commodity charge (levied upon entry and exit flows)
- TO commodity charge (levied upon entry flows)

Nigel then described the DN charges currently in place:

- DN capacity (levied upon supply point capacity holding)
- DN customer (levied upon supply point capacity holding)
- DN commodity (levied upon supply point offtake flow)

Two slides presenting payment flows in the status quo and in a post-DN sale scenario were then presented. Nigel stated that Ofgem will need to define an efficient level of NTS exit capacity product purchases. Nigel said that the price controls would need to be reopened so that DNs could recover NTS exit capacity charges from shippers, and that as a result charges to shippers would increase. He also suggested that each DN could choose how to restructure their charging methodology to recover the costs associated with NTS exit capacity, and that they could choose to adopt a variety of approaches.

As regards the NTS SO Commodity charge, Nigel said that it might be simplest, and appropriate, to leave the charge levied on shippers as at present. He stated that it may also be appropriate to leave the TO commodity charge levied on shippers as at present, but he noted that this might need to be reconsidered should the NTS charging arrangements give rise to a significant risk of over or under recovery of target NTS TO exit income.

Finally, Nigel described the impact of proposed reform on future price controls. Nigel noted that, building on the success of the entry regime, similar approaches would be adopted at exit. Therefore, the exit regime would adopt some of the features of the entry regime - in particular to provide investment signals to Transco. He went on to add that a new incentive on the release of NTS exit capacity products will need to be in place. In the DN price controls, an additional cost stream will need to be recognised and a new NTS exit product booking incentive will need to be in place.

At the end of Nigel's presentation, Sonia Brown expressed surprise at Nigel's suggestion that the price controls would be reopened as a part of DN sales. She clarified that while the adoption of Option 2A may entail an adjustment to existing revenue flows, there would be no reopening of the price control as total allowed revenues would remain the same. Peter Bingham confirmed that it was Transco's position that there should be no reopening of the price controls. Peter went on to stress that DN customers would pay higher DN charges but correspondingly lower NTS charges.