DN Sales Development & Implementation Steering Group Minutes

Meeting 25

9 November 2004, 10:00 am – 2:00 pm

Ofgem's office, 9 Millbank

Attendees

Sonia Brown	Ofgem (chair)	Robert Cross	Statoil
Jason Mann	Ofgem	Julian Bagwell	Macquarie
Sean O'Hara	Ofgem	Nick Wye	Macquarie (WWA)
David Ashbourne	Ofgem	Rekha Patel	ConocoPhillips
Liz Hillman	Ofgem	Martin Kinoulty	United Utilities
Hannah Cook	Ofgem	Beverley Grubb	SSE
Peter Bingham	Transco	Mike Young	BGT
Sue Higgins	Transco	Charles Ruffell	RWE Npower
Russell Cooper	Transco	Steve Gordon	ScottishPower
Mike Ashworth	Transco	John Costa	EDF Energy
Alan Raper	Transco	Michelle Simpson	Transco
Peter Bolitho	E.ON UK	Sharif Islam	Total

1. Review of items from DISG 24

a) Review of minutes

Peter Bolitho suggested that the reference to himself on page 2 of the minutes regarding Actions should be changed to refer to Peter Bingham.

b) Actions from previous meeting

1. Transco to set up and manage a specific issues list for licence drafting by DISG 25. Sonia Brown highlighted that this action had been tabled for DISG today.
2. Transco to give a presentation on credit arrangements at DISG 25. Sonia highlighted that this action had been tabled for DISG today.
3. Transco to provide drafting of conditions, where possible, with reference to the numbers of the current conditions in the licence. Sonia set out that Transco and Ofgem would be working to provide visibility with respect to the licence numbers.
4. Transco to present on the proposed "go live" of offtake arrangements and on the transition towards the long term arrangements. Sonia highlighted that this would be presented by Russell Cooper to the DISG today.
5. DISG participants to provide comments on Transco's proposed temporal approach by DISG 25. Sonia detailed that Ofgem had received some comments via email and that the provision of feedback by DISG participants had been tabled for today's meeting.
6. DISG participants to raise comments to Ofgem on interaction between NExAs and proposed flexibility arrangements by DISG 25. Sonia set out that Ofgem had not received any comments in this regard. Peter Bolitho

responded that he was still reviewing this. Sonia suggested that, in this case, any comments should be received by DISG 26

7. DISG members to provide comments on Transco's proposed approach to offtake flexibility. Sonia highlighted that a slot at today's DISG had been tabled for this.
8. DISG members to discuss licence conditions on LNG and non-prejudicing operation of networks at DISG 25. Sonia indicated that some comments had been received by Ofgem in this regard but that a discussion on this was tabled for later in the meeting.

2. Connections

Sean O'Hara set out some of the background in relation to Connections. He explained that in 1998 Ofgem had initiated an investigation into Transco's poor performance with respect to connections. He detailed that this had lead to the implementation in 1999 of a Gas Act Enforcement Order by Ofgem which imposed standards of service in relation to compensation payments for ICPs, IGTs and shippers requesting connections from Transco. Sean set out that in 2003 Fulcrum's performance in undertaking connections on behalf of Transco had nose-dived and that, as such, Transco had been required to pay £3 million in compensation under the enforcement order. He detailed that, in addition to this, in May 2004 the Authority had imposed £1m penalty on Transco for poor connections performance.

Sean stated that in April 2004 Ofgem had consulted on the need to replace the Order due to a potential DN sale and the need for modernisation. He explained that due to the changes to the industry that would result from a DN sale, a number of concerns had been expressed within Ofgem in relation to connections. He detailed that the April document had identified a probable need for:

- guaranteed Standards i.e. payment by the GT for every failure (not simply in relation to ICPs, IGTs and shippers) in respect of effective monopoly work, due to the problems with existing standards;
- standards in respect of timely siteworks as previously standards had focused on quotations and although these were generally provided in a timely manner they were not always of a high quality;
- application of standards to all customers as these previously only applied to those customers covered by the enforcement order e.g. ICPs, IGTs and shippers;
- improved incentive in respect of accuracy of quotations; and
- more effective auditing of quotations.

He clarified that although the April 2004 document had detailed that the changes within connections would accommodate a DN sale, these changes would be implemented even in the event that a DN sale does not proceed as Ofgem and the industry have agreed that the order is outdated.

Sean explained that the responses to the April 2004 documents were generally in support of the application of the standards to all customers, the implementation of guaranteed standards, the development of a simple standards regime and the introduction of greater emphasis on accuracy. He also set out however, that there was some disagreement on level of payments that should be required.

Sean detailed that a workshop was held in July 2004, in which more feedback was received regarding the proposed amendments to the current regime. He explained that the standards would apply to:

- the provision of quotations for new/altered connections;
- the provision of Point of Connection information to allow IGTs to fulfil their own design and connection work;
- approval of ICP designs;
- timely site-works as the present arrangements are not that effective; and
- minimum information requirements to be approved by Ofgem to minimise the number of arrangements customers are required to comply with.

Sean set out that the way forward in this respect would involve:

- the introduction of guaranteed standards (with payments) for end customers who approach GTs direct for connections. These will be introduced via Statutory Instrument (SI) under S.33AA of the Gas Act;
- the introduction of overall standards for ICPs, IGTs and shippers via a new Licence Condition (LC) as Ofgem has no vires to require payments;
- the introduction of an accuracy challenge scheme and audit requirements via SI and LC;
- the voluntary application of guaranteed standards to ICPs, IGTs and shippers in order to ensure that they do not see a difference to the way in which they are treated as compared with new customers. Sean detailed that he hoped that IDNs would also choose to take this approach but that if they did not Ofgem would have to consider approaching the DTI to request amendment of S33AA;
- Exclusions that would apply to >7 bar connections, new build housing estates connections with less than 6 dwellings and complex jobs.

Sean explained that a new Licence Condition would be included within the DN sales licence consultation which is to be published on 25 November 2004. He detailed that, concurrent with this a connections consultation regarding the new standards regime and the replacement of the enforcement order with a LC and SI as well as with voluntary arrangements would be published. He stated that this document would consider appropriate details relating to time allowed to do work and appropriate levels of payment. He also set out that this could involve the possible replacement of the enforcement order in March 2004 with new regime in advance of formal LC/SI implementation.

Peter Bolitho asked whether there would be any big surprises for Transco within this consultation document. Sean set out that he did not think there would be any as Ofgem had flagged in April that the standards would be extended to all customers and that payments for failure were likely to be similar to those for customers whose supply was disrupted. He detailed that the November document would provide interested parties with a better idea of the proposed amendments. He stated that with respect to the overall standards the bar would be set high and if performance were to slip below this, Ofgem would be ready to take enforcement action. He set out that he hoped that there would not be any problems with respect to connections but that the experience of the last few years had not given him any cause for comfort in relation to Fulcrum's performance during times of change and that if this were the case arrangements would need to be put in place to protect customers.

Nick Wye asked whether the voluntary agreements were already in place. Sean responded that the voluntary agreements would only be put in place with respect to the new arrangements and that these arrangements would only have effect when the enforcement order is revoked. Nick asked whether it would be clear from the November documents what would be put in place and Sean confirmed that the document would make clear the areas of work that would be affected and give a strong indication as to the level of payments.

Sonia suggested that DN buyers should also pursue these amendments with Transco. Peter Bingham considered that, from a Transco perspective, the amendments would be a positive development, specifically with regard to the removal of the enforcement order and the implementation of an initiative which would operate in customer interests.

3. Update from UNC Development Forum

Alan Raper set out that two UNC development forum meetings had been held in the previous week. He detailed that in the Wenesday meeting sections K, R, T and Z had been discussed and that the group had also looked at alternative wording for section P regarding top-up. He stated that on Friday the group had looked at the metering section of the Network Code and development of the transition document. He also informed DISG members that the UNC development forum had gone through the current version of the action tracker to identify the outstanding issues and that Transco were aware that further work and research would be required in relation to sections R, Z and M of the code.

Alan detailed that, during the meetings, pressure had been placed on Transco to release drafting in relation to the UNC but that Transco believed that the time would not be right to release this drafting due to the partial conclusions that have been reached within the development forum and the impact that the exit reform forum could have on the UNC. He stated that a suggestion had been made that Transco would release a sample of what the drafting for the UNC will look like in response to the concerns raised by interested parties.

Mike Young clarified that a heated discussion had taken place at the UNC development forum and that a strong preference had been expressed for sight of the drafting as soon as possible. He highlighted that if shippers were only to be given sight of the UNC in a form that is close to the final version, this would be very late in the process. He recognised that although the business rules are currently being agreed and that the drafting should reflect this, the UNC development forum remain keen to see the drafting.

Sonia stated that she thought that Transco were scheduled to release a draft of the UNC over the Christmas period. Peter Bingham responded that Transco would be releasing the business rules around this time and that, only when these had been confirmed, would it be possible for Transco to release a draft UNC. Sonia considered that the UNC development forum were only asking to see a draft of the business rules and Mike Young clarified that this would be helpful even if it were subject to caveats regarding the completeness of the rules.

Sonia Brown asked whether Transco's concerns regarding the distribution of drafting to UNC development forum members were to do with version control. Mike Ashworth expressed concern that significant changes to the draft UNC would be made as a result of the work carried out by the Exit Reform Development forum. Nick Wye considered that only about a quarter of the code would be affected by any changes implemented in this respect and that the rest could be drafted to a degree. Mike had concern regarding to what degree this could be done. Beverley Grubb indicated that about 80 – 90% of the sections already reviewed by the UNC development forum could be drafted and distributed to interested parties.

Sonia suggested that it would be in Transco's interests to comply with requests from affected parties and that if there is a strength of feeling from the UNC development forum members regarding the visibility of the UNC, then it would be sensible for Transco to go away and reconsider their position. Alan Raper considered that conducting the process in this way would be counter-productive and believed that it would be better for Transco to be allowed more time to properly determine the business rules.

Sonia asked whether Transco had commenced drafting of the UNC or whether they were waiting to decide upon the business rules and would then begin drafting on the UNC. Alan replied that Transco were looking at the baseline in terms of visibles and that these were being applied to the drafting. He stated that Transco would not want to drip feed sections of the UNC to interested parties and that this was why they had suggested providing parties with a sample of what the UNC drafting would look like in draft form. He also had concerns that Transco could end up in a version-control nightmare. Mike Ashworth suggested that Transco could release draft versions of the UNC with category 1 changes (e.g. name/reference changes) included. He considered that the key objective would be to make parties comfortable with what the UNC would look like in an environment with more than one transporter. Beverley Grubb was of the opinion that the UNC development forum would want to see more than references to Transco simply amended to relevant transporter.

Sonia suggested that Transco should go away, consider its roadmap and take on board the comments that people have made. She emphasised that the development of the UNC is supposed to be a process of consultation and that parties who have participated would want to feel like they had been given adequate time to consider the drafting. She also considered that people would want to be given more detail of what the sample drafting would consist of before they expressed their support for a solution of this nature.

Beverley Grubb also detailed that people need to understand at what point the full legal drafting will be released as, at present, the timeline shows it being released during a two month period and that more clarity would therefore be required in this respect.

Action: Transco to provide an update regarding the approach it will follow in relation to the release of legal drafting for the UNC.

Action: Transco to provide an update regarding an approximate date on which the legal drafting would be released.

Nick Wye stated that his expectation was that Transco would provide a first draft to interested parties and that, following the receipt and consideration of responses, it would then provide the final draft of the UNC. He therefore did not understand why issues regarding version control would be experienced as part of this process. Mike Ashworth set out that these issues related to further concerns that could be identified through the UNC development forum process. Sonia Brown also highlighted that, as a result of modifications proposed and implemented within the Network Code, the baseline would be moving. Nick suggested that the development forum could work on the basis that Transco would be amending version 3.09 of the Network Code and that they would accept that this would change over time but that they would continue to work on this basis.

Sonia suggested that Transco should go away and consider the points presented and then present their position at DISG 26.

4. Standards of Performance

Sonia set out that Standards of performance would be relevant to Ofgem's November licence consultation and that, as such, it might be helpful to set out Ofgem's thinking to provide interested participants with a clear understanding of the issues.

Jason Mann detailed that the presentation would concentrate on issues regarding quality of service and set out that there are three workstrands which interested parties should be aware of in relation to this and that these would be addressed in turn:

- August consultation paper on quality of service;
- New licence condition for assessing quality; and
- Amendments to Overall Standards of Performance.

Jason set out that Ofgem had published a document for consultation in August 2004 regarding quality of service issues in gas distribution. He stated that while respondents were generally supportive of Ofgem's intention not to introduce financial incentives on non-contractual interruptions, energywatch had expressed concerns that quality may deteriorate post sales without explicit incentives/monitoring. Jason detailed that following consideration of the responses received to the consultation, Ofgem intended to retain the existing regulatory framework for remainder of price control period (i.e. RIGs reporting, Standards of Performance etc.).

Jason set out, that Ofgem has also proposed to introduce a new licence condition which would assess the quality of service provided by DNs and would require DNs to carry out regular customer surveys. He explained that Transco already undertakes similar surveys for internal management purposes and that it is Ofgem's intention to formalise this approach through the licence. He detailed that the obligation would only require DNs to report results and that, as such, no revenue would be exposed.

Jason set out that a survey approach would require transporters to provide information to Ofgem and wider stakeholders regarding customers' satisfaction with respect to quality of service on an ongoing and consistent basis. He detailed that the survey would cover customers' satisfaction with a range of attributes following planned or unplanned interruptions including communication issues and any inconvenience caused by the interruption. He explained that drafting of the licence condition would be completed by 12 November and that it would therefore be presented at DISG 26. He also stated that the licence condition would also be consulted upon as part of the November DN Sales consultation.

Jason detailed that the Overall Standards of Performance (OSOPs) would require re-determination by the Authority for each new DN owner and set out that Ofgem has also become aware that some 'technical' changes to these will also be necessary. For example, OSOP1 on call answering may need modifying to reflect that Transco will be the only transporter responsible for the operation of the national emergency number. He stated that Ofgem intends to consult on these amendments later this year.

Sonia Brown summarised that the new licence condition would be put in place to ensure that Transco's current standards of performance are maintained by DNs. She detailed that current determinations may also be carried across and that these could include a number of associated technical determinations. She confirmed that a document regarding this process would be issued later in the year.

Julian Bagwell asked whether the treatment of determinations would be dealt with separately to the licence consultations. Sonia responded that the licence consultations were simply intended to look at the licence conditions in isolation rather than including any wider determinations that it may be necessary to make.

Sonia set out that Ofgem planned to issue these licence conditions to DISG 26 and that this would close off a longstanding action on Ofgem.

5. Credit

Michelle Simpson opened the presentation by introducing herself as the Credit Risk Manager for Transco. She set out that the presentation was intended to look at the type of security cover that would be required with respect to the UNC going forward and that the presentation had incorporated two main assumptions:

- that section S of the Network Code will remain the same; and
- that the credit cover rules included within the existing Network Code will be replicated.

Michelle detailed that she was working on the assumption that hive-down of the IDNs would take place on 1 May 2005. She explained that, under the Network Code there is a requirement on Transco to provide 63 days of security and that this obligation would cover the period including March and April. She also set out that there will be a similar requirement under the UNC and that, as such, 63 days worth of security would need to be provided for the period of May and June. She confirmed that while under the UNC the beneficiary would be limited to Transco, under the new UNC the beneficiaries would include Transco plus the four IDNs. Michelle also confirmed that 12 month credit holdings would continue to be required in relation to LTSEC.

Michelle stated that the March invoices under the Network Code would be issued between 5 – 30 April and would be due between 20 April and 15 May while April invoices would be issued between 5 – 31 May and would be due between 20 May and 15 June. As such, she explained that all invoices and adjustments issued under the provisions of the Network Code would cease around 15 June. She set out that on an ongoing basis after this date, the only adjustments to invoices under the Network Code would be made on an ad-hoc basis.

Michelle detailed that the Security provisions that would need to be in place under the Network Code for the interim period would include:

- the continued availability of Network Code security until the end of June 2005 as the invoices under the Network Code will not fall due until then;
- residual Network Code security for remaining adjustment items, although after June the obligation to provide this would cease;
- implementation of security arrangements for UNC by 1 May 2005 including five separate security documents for each company registration number;

Sonia pointed out that if Transco is required to legally separate, it will form six entities and therefore require six separate security documents.

- Transco is prepared to accept joint security to cover all Network Code charges and UNC exposures to cut down on the volume of documents that will be published around May 2005;

Peter Bingham highlighted that this would be done to the extent that it would be permitted following legal separation. Michelle set out that it would be possible for more than one company to be put on an invoice but that this would be dependent upon the receipt of consent for this activity from relevant banks.

- Transco total security review could take place in July 2005; or
- users could elect to leave their Network Code security arrangements in place and implement separate securities for UNC obligations and subsequently review Network Code security in July 2005.

Michelle stated that there were three options under which security arrangements could be accommodated following a potential DN sale. Under option 1, with respect to the Network Code Transco would be required to offer 63 days of credit cover which would run for the period of March and April and would require security cover of £2 million. While under the UNC, during the period of May and June, £1 million of credit cover would be required to accommodate the obligation to provide 63 days of security. She set out that, under this option, the total security to Transco would sum to £3 million.

Michelle detailed that the option 2 approach would allow recognition of the fact that the majority of the April and March invoices would be paid before this date even though the security cover will be required for a period of 63 days,. She stated that assuming that 50% of the invoices will have been paid, the security required under the Network Code will be reduced to £1 million. She set out that the situation with respect to the UNC would be the same as under option 1 and that the security required would be £1 million. She summarised therefore that the security required under option 2 would be £2 million and that a review of this figure would be carried out in July 2005.

Michelle set out that option 3 would involve a situation in which no security cover would be required under the Network code to cover the period of March and April and that the total security to Transco would be £1 million. She outlined that this option would not be a workable solution.

She therefore set out that Transco had chosen to recommend option 2 as the most appropriate approach to security cover as there is a belief that this would cut down on the number of documents and level of security required. She stated that option one would be a good option if Transco were of the opinion that the current level of security should remain in place.

Sonia Brown noted that under option 2 it would appear that the users of the sold networks would also need to securitize and that this was not illustrated on the UNC side. Michelle responded that £1 million of securities would also be held by the sold networks, as well as the £1 million that would remain with Transco and clarified that this was why securities to Transco had been reduced by £1 million under the UNC. Jason clarified total credit required would fall from £4 million under option 1 to £3million under option 2 and Michelle confirmed that this was correct.

Sonia asked whether Transco would require a Network Code modification with respect to the 63 day rule, under option 2 and Michelle replied that they wouldn't. Sonia asked what would determine that Transco would not be required to comply with the obligation to provide 63 days worth of credit. Michelle responded that the obligation was worded in such a way as to allow for the security arrangements to be slightly amended as long as adequate security cover is available. She detailed that a number of companies would not be affected by the change in security arrangements including:

- companies with an investment grade rating; and
- companies on a pre-payment agreement.

She stated that the only companies affected would be those that are required to provide security documents to Transco.

John Costa asked at what time companies would need to be compliant with the amendments to the current security arrangements. Michelle responded that the relevant amendments would need to be in place by 1 May 2005 and that as soon as the business rules had been determined Transco would be in a position to send affected parties details of what the credit requirements will be. John asked whether affected parties would continue to operate under the existing arrangements until 1 May 2005. Michelle replied that the arrangements would be determined three months prior to hive-down and that it will be at this point that Transco will begin to send out details regarding credit requirements. She detailed that the requirement to attain 63 days of security would remain.

Sonia asked how the companies would be operated between hive-down and completion of the share sale. Michelle responded that the IDNs would be operating as separate entities under their individual company registration numbers. Sonia asked whether Transco would be working with the IDNs in relation to security arrangements to ensure a smooth handover of obligations. Michelle responded that Transco had consulted with the relevant buyers and that they are content with the process that will be followed.

Martin Kinoulty raised a process point and highlighted that the presentation that had been given to the DISG was not the one that he had been expecting. He detailed that the action that had previously been placed on Transco with respect to credit had been in relation to credit terminations and whether Transco intended to implement a one-out all-out condition. Sonia confirmed that this was not the presentation that she had been expecting either. Peter Bingham pointed out that the presentation that had been given was in relation to an area of concern to shippers. Sonia acknowledged that she was not disputing the relevance of the presentation but outlined that a whole host of other issues remain which will need to be resolved. She set out that a number of actions had previously been placed on Transco in this regard and that these actions had yet to be met.

Action: Transco to respond to the actions placed on them at DISG 20 to undertake a presentation to DISG members regarding credit arrangements.

Martin Kinoutly stated that if the position that Transco presented at DISG 20 is the approach that they intend to take then the DISG members will need to be aware of this and set out that equally, if this is not the case, the relevant proposals would need to be brought to the DISG. Peter Bingham was not sure that Transco would have any further amendments to add to the termination arrangements. Sonia outlined that a number of issues still remain outstanding and that these would need to be addressed. Peter set out that Transco would re-visit these issues and report back to the DISG. Sonia suggested that it may be helpful to do this via Ofgem as they may have comments in this regard, as well as comments regarding the implications that Supplier of Last Resort arrangements may have for credit terminations.

6. Exit Reform Development Forum

Peter Bingham set out that the first meeting of the Exit reform development forum would be held on 11 November and that six or seven weekly meetings of this group would be held in the period leading up until Christmas. He detailed that the objective of the meetings would be to bring relevant stakeholders up to speed and provide them with a high level view of the principles and detailed business rules regarding the exit regime. He stated that the meetings would also allow Transco to provide stakeholders with further explanation of the regime and a clarification of the proposals, as well as enabling Transco to receive some feedback on the proposals presented. He explained that the process would allow Transco to refine its proposals ahead of the formal consultation on offtake arrangements and exit regime.

Peter Bingham set out that a lot of work would be required, that the material that would be presented within the forums would be challenging and provided an overview of the way in which the meetings would be structured in the coming weeks.

Sonia Brown asked whether Transco could confirm that the constitution of the group would be the same as the UNC development forum. Peter Bingham responded that a set of business rules would be established to engage interested parties and develop the best possible product. He detailed that the process would be 'fit for purpose' and that it would mimic the UNC development forum. Peter Bolitho expressed disappointment that these discussions would not be held via the UNC development forum.

Julian Bagwell asked whether the decision had yet been taken regarding whether the rules would be contained within the UNC or a separate offtake code. Sonia responded that a decision in this regard had not been reached but that the working assumption would be that the offtake rules would be contained within the UNC. Julian asked whether the business rules for the exit reform development forum would be published in January. Peter Bingham responded that they would. Julian asked whether the business rules are currently sufficiently developed to allow drafting of the relevant sections of the UNC to commence. Peter Bingham responded that many of the business rules have been extensively developed but that these will be subject to agreement through the exit reform development forum and that, following agreement, these rules would be sent to Transco's legal department for drafting.

Peter Bolitho asked whether a separate modification to the Network Code would be necessary to support the amended exit arrangements or whether these amendments would be considered integral to the UNC. Peter Bingham responded that the amendments would be considered integral to the UNC as they would be necessary to support a divested industry structure.

Beverley Grubb asked whether the technical offtake provisions would be outside of the UNC. Sonia responded that these provisions would be contained within an ancillary contract and that they would form a bilateral contract between the DNs and the NTS. She detailed that, as such, parties that would not be affected by the contract would not be able to modify it. Peter Bolitho considered that this could be seen as a new development and that shippers had always maintained an interest in being able to modify the rules contained within the Offtake code. Sonia responded that shippers would not have a direct role in these provisions and outlined that a distinction remained between the arrangements that shippers will be involved in and those that they will not. She outlined that where arrangements would be part of the commercial regime, they would be contained within the UNC and subject to modification rules. She set out that a set of issues had previously been discussed at the CIWG and a decision been reached by its members that operator to operator arrangements should be contained within a set of bilateral contracts between the NTS and the DNs. She detailed that anything that users would have an interest in commercially would remain within the UNC. Peter Bolitho expressed agreement with this and stated that provided that visibility was retained with respect to this issue, this would provide comfort to shippers. Sonia suggested that it could be helpful for Transco to make it clear to interested parties which provisions would be contained within the bilateral contracts. Beverley Grubb agreed, pointing out that it had been a long time since issues of this nature had been discussed and that it would be helpful to gain an initial view of which provisions would be contained within which sections of the contracts. She also detailed that this information should be fed back to the UNC development forum and Alan Raper agreed that this would be sensible even if the provisions would not have an effect on the work of the UNC development forum.

7. Temporal definition of exit rights (feedback)

Sonia Brown set out that this presentation had been given to DISG 24 and that as the proposals contained within the presentation had been new to DISG members, they had been given some time to think about any concerns or implications that the proposals may have. Sonia also stated that she would circulate the comments that Julie Cox had submitted to Ofgem in relation to this issue.

She considered that DISG members may have related concerns surrounding the sub-annual product and whether allocation of capacity in this way would be appropriate.

Charles Ruffel asked what the concern in this regard would be. Russell Cooper outlined that the chief concern that may arise would be in relation to the complexity of the allocation process. He detailed that, as part of the process, Transco would need to attain an understanding of the signals that it would receive from shippers and that, in this respect, as shippers would be required to enter bids for allocation of capacity this may change Transco's assessment of where the capacity should be allocated. He stated that price instability in relation to a sub-annual product is an area that may also cause concern.

Peter Bolitho set out that the usefulness of having annual products and near-term products would be an important factor in decisions reached in this regard.

Sonia Brown asked what the general view of the DISG members would be and asked if anyone would disagree. She noted that no disagreement had been expressed. Peter Bolitho pointed out that the fact that no disagreement had been expressed did not constitute an endorsement of the proposals as shippers are generally happy with the product that they already have.

Russell Cooper pointed out that as these arrangements would be placed within the UNC it would be possible for any party to raise a modification to the way in which they operate. Charles Ruffel asked whether there was a presumption that if Transco has the ability to offer a long-term interruptible product, they would also have firm capacity available. Russell asked for clarification that this was a reserve price issue and Sonia detailed that if it was that it had not yet been dealt with. She stated that only the temporal definition of the product had been addressed and that issues regarding the reserve price had yet to be determined.

Russell Cooper confirmed that, subject to willingness to pay, demand for flexibility could be a driver for investment under the proposed arrangements.

John Costa asked how the availability of interruptible capacity would fit in with the current transporter licence condition to only offer firm capacity. Sonia responded that the licence condition was being removed as part of the section 8AA licence modifications.

8. Flow flexibility (feedback)

Sonia Brown detailed that Transco had given a presentation to DISG 24 regarding flow flexibility and that they would be happy to answer any questions that DISG members have in order to improve understanding of the proposals. Russell Cooper stated that the proposals had not received a great deal of interest but that issues that had been raised in this regard had focussed mainly on the complexity of the process. Peter Bingham set out that the uncertainty and related concern regarding the cost of such arrangements was understandable.

Russell explained that a basic question that some respondents had posed was in relation to the benefits that Transco would achieve as a result of the new arrangements. He detailed that, in this respect, Transco would be able to achieve a better idea of users' demand profiles and that action will need to be taken by Transco to meet these demands. He set out that, as such, in this respect, the arrangements would provide Transco with advance notice of the level of flexibility required. John Costa pointed out that Transco already receives advance notice in relation to the construction of a power station. Russell responded that this would not provide Transco with an idea of what within day demand may be. Sharif Islam considered that Transco would already attain an estimate of demand from ARCAs. Russell replied that while these provide Transco with details of ramp rates and notice periods, flexibility is a banking arrangement whereby users will be borrowing stock from the pipeline and this is different from ramp rates or notice periods.

John Costa stated that he did not see how these arrangements would be different to those that are already in place. Russell replied that obligations such as 'reasonable improvement' could be better met through the provision of improved information. Beverley Grubb perceived that if Transco's concern was mainly focussed around the provision of accurate information then this constituted a complicated way of obtaining that relevant information. Russell detailed that the problem with simply requesting information from shippers was that unless a financial commitment to the information is involved then the quality of information is not generally as good. He set out that Transco would want to make investments based on the information that is received and that they would therefore need to be confident that the information was accurate. Beverley considered that, in relation to the submission of information, it would be helpful for shippers to understand what type of investment Transco were planning to make and whether this would be in relation to flexibility or in relation to pipelines etc.

Russell stated that discrimination could also be an issue if the current arrangements were transferred into a post-DN sales environment. He detailed that, at present, flexibility is offered as a bundled product and that DNs are currently allocated flexibility to allow them to comply with the obligation to achieve 'reasonable improvement' but that, following a potential DN sale it would be possible to free up DNs to the level of flexibility that power stations currently enjoy. He explained that in such a situation it would be necessary to operate a sales process to determine which party would place a higher valuation on allocation of the flexibility.

Russell also highlighted that IDNs may want to a change to be made to the way in which flexibility is operated in order to have access to increased levels of diurnal storage and that to allow this, IDNs may be required to contribute to increased levels of investment. He set out that, under this approach, it would be possible to source additional flexibility from within the networks and that it should not be the case that Transco has the ability to pre-judge the preferred arrangements with respect to diurnal storage, on behalf of other parties. Sonia highlighted that if flexibility were to be priced at low or no cost then a number of parties would demand flexibility at this cost, but she set out that if charges were set to a higher level, then a reduced number of parties would want to purchase it. She explained that this approach would allow interested parties to have confidence that Transco was not discriminating in its allocation of flexibility.

Nick Wye asked how Transco intended to price the flexibility product. He also highlighted that the presentation to DISG 24 had suggested that flexibility would be a one-way product and asked whether, if users provided flexibility to Transco, they would be paid for doing this. Russell explained, in relation to the first question posed, that Transco had built its systems to be capable of providing the basic capacity demanded by users to them and that flexibility is simply a by-product of this. He set out that the capital invested to pay for additional NTS capacity is sourced from TO revenue and that the price currently charged in relation to the allocation of a flexibility product is low to zero. He detailed that it would be the responsibility of the SO to make diurnal storage available and allocate it to the relevant users but that the responsibility to respond to demands for additional diurnal storage at a particular time would lie with the TO. Sonia considered that Transco would likely already have indicative figures in this regard as their initial set of rules had provided an account of what their plans would be. She also set out that Transco would be aware of the level of flexibility that NTS direct connects currently demand and that Transco should therefore simply be able to sum these numbers. Russell said that he would look into this going forward.

Nick Wye asked whether the way in which Transco would value linepack would be transparent. Russell responded that Transco would be willing to buy back flexibility from NTS direct connects and that the process regarding the buy-back of capacity would be written into the UNC rules.

Peter Bolitho asked whether it would be necessary for users to purchase the flexibility product before they were able to use it. Russell responded that if shippers were to request additional flexibility, Transco would invariably be able to provide them with it and highlighted that this would be effective in minimising balancing costs. Peter Bolitho considered that the requirement to acquire flexibility in advance would introduce rigidities into the process and that the requirement to plan ahead may introduce inefficiencies. Sonia highlighted that DNs could be constrained in their access to flexibility by Transco under the new arrangements but that DN owners may be unwilling for Transco to limit the amount of flexibility that they are allocated. Peter Bolitho responded that as an end user he did not consider that shippers should not be compared to transporters. Sonia pointed out that Peter had argued that he would want to be involved in all bilateral agreements with respect to the UNC but that he was taking the opposite view with respect to this issue in that he did not want to be affected by DN-related activities and that he was arguing that comparisons between DNs and shippers should not be made. Peter Bolitho considered that the issue of flexibility was an operational matter and that this should not be compared with processes in relation to the UNC. Jason Mann pointed out that the issue of flexibility was not an operational matter but a financial matter as to obtain additional flexibility DN owners would have to invest in it.

Russell Cooper clarified that Transco and Ofgem were not trying to introduce complexities within the arrangements and that if flexibility products were available at low to zero cost then it would be possible for shippers to purchase these products at this price. He set out that there is always an issue with respect to the prices that will be charged and explained that Transco were simply trying to find a way of doing this that would be equitable. Peter Bolitho emphasised that the requirement to forecast demand for flexibility in advance would introduce rigidities into the process. Sonia suggested that Transco should think about the interaction of balancing mechanisms and investigate whether any changes would need to be made to the current processes. She also acknowledged that the new arrangements could affect the competitiveness of parties, citing that if an entity were able to acquire flexibility on the day-ahead market and were then to bid into the market it would be in a better position that another entity that purchases flexibility on the day and incurs overrun charges. Nick Wye considered that it would be difficult to bid in at the day-ahead market and Sonia responded that for this statement to be true it would require some assumptions to be made about the state of competition. Nick clarified that he was simply highlighting that the processes should be simple and Sonia agreed that this should be the case.

Beverley Grubb asked whether a relevant assumption would be that flexibility would be operated on a baselines per node basis. Sonia responded that there were some problems in relation to this approach which Ofgem and Transco would need to consider and she therefore stated that this should not be an assumption should not be made.

John Costa set out that this alteration in flexibility arrangements would be a fundamental change to the way in which the flexibility product is operated and that he had two outstanding issues in this respect. He detailed that the first was in relation to the constraints that this amendment may place on the electricity industry due to a potential increase in the price of electricity that may be experienced and set out that this had been discussed at last weeks DISG but that it had not been included within the minutes. Sonia clarified that the change in arrangements could affect the competitiveness of companies in relation to their ability to bid into the market but set out that if companies could achieve a competitive advantage in this respect then this could change their behaviour. John Costa stated that his second issue concerned which option, in relation to diurnal storage, would be included within the Final IA. Sonia responded that the final IA would include the diurnal storage base case. John asked whether Ofgem had come up with a level of costs associated with this and Sonia replied that the Final IA would capture the overall level of costs associated with a potential DN sale against the overall level of benefits.

Sharif Islam expressed concern that the amendments to diurnal storage outlined by Transco would be used as a lever to argue that the SO should allocate priority access to diurnal storage to the DNs. Peter Bingham set out that this was not Transco's intention and that the proposals were simply intended to support a potential network sale.

Peter Bolitho considered that the number of locations may make it difficult for Transco to maintain a measure of the amount of flexibility used. Sonia asked whether Peter would want to have an offline discussion about this and he confirmed that he would.

9. Getting to day one

Russell Cooper explained that this presentation would provide a description of the way in which the new arrangements in relation to exit capacity and diurnal storage would be put in place and how any required interim arrangements would be addressed.

Russell set out that the proposed reforms to NTS allocation of exit capacity would apply from 2008 but that the opportunities to obtain allocation of NTS Exit Capacity and Diurnal Flexibility for 2008 would be available from summer 2005. He detailed that the products obtained during this period would be available for use from 2008 onwards and that in accordance with this, the associated billing arrangements would apply from 2008. He stated that interim arrangements would therefore apply during the period from May 2005 to summer 2008.

Russell explained that NTS Exit Capacity and Diurnal Flexibility would be offered through three types of allocation:

- Long Term (years +3 to +n) - Unconstrained
- Medium Term (years 0 to 2) - Constrained
- Short Term (Day Ahead and Within Day)

He detailed that Transco's proposals for the allocation of products for 2008 were that:

- the first opportunity for users to demand long term products would be in summer 2005;
- the first opportunity to obtain medium term products would be in summer 2006;
- the second opportunity to obtain medium term products would be in summer 2007; and
- the first opportunity to obtain short term products would be during 2008.

Russell also explained in more detail the sequence in which users would be able to obtain allocation of NTS exit capacity and diurnal flexibility from summer 2005.

He set out that during the interim period, interruptible and firm capacity rights would still be available to users as they are now and clarified that there would not be any change in the arrangements for NTS direct connects or shippers to acquire exit capacity or flexibility. He detailed that users would simply be offered the choice to submit demands for long-term capacity if they so wished.

Russell explained that some uncertainty exists regarding whether, in the interim period, DNs should demand exit capacity from day 1:

- Under option A – under this approach DNs would be required to register with the NTS for the exit capacity that it would need and would pay the NTS for this capacity. The DN would also be required to develop a revised pricing methodology to reflect charges made to shippers for allocation of the relevant capacity. This approach would more closely reflect the desired objective to achieve an "independent" DN.
- Under option B – under this approach DNs would be allocated a baseline capacity and shippers would register their capacity at the relevant supply point. Shippers would then make a payment to the NTS or DN for the relevant NTS exit capacity. This option would require minimal change to the current regime.

Russell set out that the implications of the implementation of both options were being explored to ensure that they would not have any untoward effects on any other market arrangements. He also detailed that in both cases, incentives would act upon the NTS and DNs for the efficient release and demand of capacity.

Peter Bingham asked whether, under option B, DNs would still be able to demand additional exit capacity, over the allocated baseline capacity, from the NTS and Russell responded that DNs would be allocated further capacity subject to availability.

Nick Wye asked when the baseline for DN capacity, under option B, would be set. Sonia responded that it had already been set and Russell detailed that the Baseline capacity would be based upon the requests already submitted to the NTS.

Julian Bagwell asked whether DNs would be committed to the capacity that they had requested in 2005 or whether it would be possible to trade on this. Sonia responded that DNs could engage in facilitated trade through Transco.

Robert Cross asked whether NTS direct connect booking arrangements would remain the same and Sonia confirmed that they would. Nick Wye noted that during the interim period DNs would be buying exit capacity from the NTS and asked whether this would be allowed for through the price control. Sonia responded that the impact of this on the price control would depend upon which option was adopted.

Beverley Grubb asked which would be the base case for the payment options and Sonia responded that this would be option A as this approach was the most similar to the long-term arrangements that would be implemented.

10. Licence issues list

Sue Higgins set out that the list of licensing issues that she had distributed was a first draft and that she would be interested in receiving any feedback regarding the format or the comments that have been raised.

Peter Bolitho suggested that it would be useful to have the main points highlighted in bold. He also set out that the comments from EON regarding the ability to change the provisions of the Network Code were made in response to the placing of the offtake code within square brackets within the licence drafting. Sonia responded that it was Ofgem's current position to place all of these arrangements within the UNC itself.

Martin Kinoulty asked for clarification regarding what exactly the licensing issues list was attempting to include. Sonia responded that it was intended that the list would provide details of comments made regarding licensing at DISG meetings, to Ofgem via email and to Transco. Martin acknowledged that the point had already been made at the DISG but highlighted that the drafting in licence condition 4A was worded as if to have the effect that the charging methodology would be kept 'at all times under review' and asked for clarification regarding how this would work. Sonia responded that this wording is currently included within NGCs existing licence and should not therefore be too onerous for gas transporters. She clarified that it would simply require transporters to operate a sensible compliance programme.

Sonia set out that Ofgem would be managing the process associated with the actions arising in relation to the licensing process and the replies that would be made in relation to issues raised. She detailed that Ofgem would be publishing its next licence consultation in November and a follow-up section 8AA consultation document in February. She explained that prior to this an intensive period of licence drafting would be taking place leading up to the Authority meeting in January. She considered that, assuming consent to the proposed DN sale was received the DISG meetings, following the Authority's decision in January, would be used to discuss the licence drafting.

Peter Bolitho stated that he had an issue regarding the licence drafting in relation to the charging methodologies. Sonia responded that these issues had been raised in E.ONs response to Ofgem's informal licence consultation and that a response to these comments would be included within the November licence consultation. She set out that Ofgem had been considering the necessary number of changes to the charging methodology per year and that it had become aware that changes may be required twice a year to reflect an option 2A approach with respect to offtake arrangements.

Sue Higgins stated that if DISG members were to think of any comments regarding the licensing drafting issues list then they should send these to Ofgem and, if possible also forward them onto herself.

Action: DISG members to check all of the issues included on the licence drafting issues list and circulate any comments to Ofgem and to Sue Higgins at Transco.

Sonia asked whether it would be possible for Transco to number all of the licence conditions that they had drafted according to the existing condition within the licence which they currently represent.

Action: Transco to number the licence conditions that have been drafted, according to the numbers of the existing licence conditions that they represent.

Sonia suggested that after the publication of the November licensing document it may be possible for some of the issues on the list to be closed. She detailed that In January the DISG would be responsible for ensuring that the licence drafting adequately reflects the relevant policy positions and that the drafting is ready for the Section 8AA consultation which is to be released on 14 February.

Julian Bagwell asked whether comments should be sent to Ofgem or Transco and Sonia responded that as long as the responses were not confidential it would be helpful for respondents to send them to Transco and Ofgem.

10. Licence conditions (feedback)

Sonia set out that at DISG 24 an overview had been provided in relation to the licence conditions regarding the gas transporters general obligations in respect of its pipeline system and asked whether any of the DISG members had any comments in relation to this.

Beverley Grubb expressed concerns in relation to the generality of the drafting. Sonia replied that she understood these concerns but stated that the licence drafting had been based upon the drafting included within the shippers licence in relation to a similar obligation. She considered that shippers currently comply with the requirements of this licence condition and given that similar wording is used in this regard it should not be a problem for transporters to comply with the drafting set out within this condition. Julian

Bagwell was also of the opinion that there may be some problems with the drafting of this condition.

Sonia detailed that her personal view was that she was not sure that the obligation on transporters to provide, develop and maintain should be included within the drafting. Sue Higgins responded to this and set out that this is where comfort would be attained by shippers. Beverley Grubb indicated that she thought that this had been attained elsewhere within the licence drafting. Sue asked whether some examples of where problems with respect to this obligation would arise. Sonia replied that she did not consider that the DNs should be treated any differently from shippers and, as such, that they should not be required to provide, develop and maintain such services. Martin Kinoulty set out that given that there are other licence conditions that deal with these issues, he did not consider that it would be necessary to include this obligation.

Peter Bolitho detailed that shippers had not agreed to the implementation of some of the relevant shipper conditions within their licence and that he did not consider that it would therefore be appropriate to simply transfer the obligation to transporters. Sonia suggested that DN buyers should submit their views to Ofgem regarding why they should be treated differently to shippers in relation to this licence obligation. Nick Wye stated that it would come down to the fact that information would be provided from shipper to transporter as opposed to the situation under this licence condition in which in which information would be passed from transporter to transporter. He therefore questioned whether a cut and paste would be appropriate. Sonia responded that if the DN were to provide false and misleading information this could have potentially more serious consequences than if a shipper provided such information and she considered that this was why it would be prudent to include this obligation within the transporter licence. Nick did not think that an obligation of this nature would provide an appropriate incentive in this regard.

Sonia also highlighted that another set of amendments to Standard Conditions and Standard Special Conditions had been presented at DISG 24 in relation to the licence amendments necessary to reflect arrangements regarding LNG. She indicated that Ofgem had not seen any comments in this regard as yet and outlined that she was not surprised by this in view of the fact that the drafting was simply intended to reflect the structure that will be in place with respect to LNG in a post-DN sales environment.

Peter Bolitho stated that on page one, paragraph one of this licence drafting he had some issues regarding the definition of equivalent purpose and asked for clarification as to whether this was an energy issue or a constraint management issue. He detailed that he considered that this definition may be too broad. Sonia explained that the licence condition was referring to the transporters LNG business and clarified that the NTS would want to be able to use this for energy and constraint management purposes.

12. Any other business

John Costa set out that Ofgem had stated at DISG 24 that at DISG 25, attention would be given to system implementation. Sonia acknowledged that this had been the case but stated that she thought that it would be important for Russell Cooper to explain the interim arrangements that would be in place from day 1. She detailed that Transco would update the DN sales roadmap to reflect the interim arrangements and the timing of the first auctions for DISG 26.