Enduring Offtake Arrangements Working Group

Meeting 5

24 February 2006, 13.15 - 16:00

Ofgem's office, 9 Millbank

Attendees:

Robert Hull	Ofgem (Chair)	Eddie Profitt	MEUC
Matteo Guarnerio	Ofgem	Phil Lawton	NGD
Suzanne Turner	PA Consulting	Mark Freeman	NGD
Jason Mann	PA Consulting	Bethan Winter	NGD
Tim Dewhurst	PA Consulting	Steve Courtney	SGN
Roddy Monroe	Centrica Storage Ltd	Nick Wye	Waters Wye Assoc.
Stuart Waudby	Centrica Storage Ltd	Phil Broom	Gaz de France
Christiane Skyes	E.ON Uk	Gareth Evans	Total
Avian Egan	BGN	Derek Russell	Viridian
Alison Russell	Centrica	Nigel Sisman	NG NTS
Mike Young	Centrica	Elaine Calvert	NG NTS
Claire Beausang	CER	Peter Dickinson	Ofgem
Julie Cox	AEP	John Bradley	Joint Office
Steve Rose	RWE Npower	Mick Curtis	$E=mc^2$
Paul Roberts	NG NTS		

Introduction – review of minutes and actions

Jason Mann welcomed the group and asked whether anyone had comments on the minutes of EOWG4. Derek Russell noted that some of the comments he had raised at EOWG4 were not reflected in the minutes of the meeting. Derek said that he would send an email to Ofgem to outline these comments.

Action: Ofgem to amend EOWG 4 minutes to include Derek Russell's comments

Jason then reviewed the actions that were taken in EOWG 4:

- *Ofgem to amend EOWG 3 minutes to include Derek Russell in the attendees list.* Closed
- *NGG to undertake more work on the transmission/flexibility substitution ratio.* Ongoing
- *NGG to consider methods for allocating additional flexibility in the short term.* Ongoing
- *EOWG participants to consider their individual offtake profiles.* Ongoing
- *NGG to finish presentation on firm capacity booking at EOWG 5.* Closed
- *NGG to consider whether different types of users impose different costs to the system.* NGG stated that analysis undertaken to date has shown that they are not aware of any reasons why different types of users can impose different costs to the system.

Long term allocation of capacity

Paul Roberts gave a presentation in which he provided some worked examples on how different options for allocation of capacity in the long term could work in practice.

First, Paul provided some examples of how option "U1" (the "reservation agreement" approach would work). Mike Young noted that, if capacity requests are below baseline, users should be able to obtain capacity within lead times.

Paul also clarified that under this option users have rolling rights and they need to proactively notify the transporter only if they want to increase or decrease their capacity holdings. Paul noted that under this option there would be a registration process one year ahead but parties would be able to lock in their capacity rights earlier via a reservation of capacity. Paul noted that this option is very similar to the status quo (dependent on the duration of x,y,z), although it would provide a common framework for the reservation of capacity (requiring a common level of commitment from all users).

Some participants questioned why the level of commitment required should be greater than that provided in the Langage ARCA (i.e. one year). Paul replied that there have been ARCAs with a level of commitment different from one year in the past. Also, Paul noted that the model has only parameters at the moment, and is intended to provide a common framework for user commitment, but the precise level of user commitment required needs to be agreed.

Alison Russell asked whether under this model users were required to commit to pay only for the capacity triggering the investment (ie incremental capacity) or for all the capacity. Paul Roberts said he would check how this issue is dealt with for the transitional period.

Action: NG NTS to confirm whether ARCA user commitment in the transitional period applies only to capacity triggering investment or to all capacity

Paul then outlined some worked examples of option U2 (which in previous presentations was described as the "extended registration period" option). Paul noted that if a user makes a rolling commitment of 'z' years, they would be guaranteed capacity. Mike Young noted that the examples provided were relevant for the first allocation, but that then capacity offered in previous allocations would not be on offer. Mike also noted that this model would require users to commit as far forward as possible in order to secure their rights. Peter Dickinson replied that this is not necessarily the case, as some users may prefer to take some price risk and wait.

Mick Curtis noted that under this model there may be a situation in which one user is requesting capacity within baseline and obtains it. However, if another user comes in, the first user may not obtain the capacity requested because he has not provided a sustained signal of "z" years of capacity requests. Mick noted that there should be a mechanism by which the user is informed that another user has booked at that node and that a sustained demand is requested so that users can make a rolling 'y' years commitment in advance of a constraint occurring and then commit to 'z' years. Suzanne Turner agreed that such a mechanism would seem sensible.

Paul also outlined some examples under which incremental capacity is requested, but some users do not provide sufficiently sustained demand for that capacity (i.e. do not book the required level of incremental capacity for "z" years). Elaine Calvert noted that users may still obtain the capacity requested if NG NTS decides to release it as non-obligated capacity. Paul recognised that this is a possibility. However, he noted that users who have not provided sustained demand for incremental capacity would not be guaranteed their capacity. Paul also outlined an alternative sub-option, under which capacity requests at a particular node would be aggregated. Paul noted that in some cases aggregation would allow NG NTS to allocate incremental capacity more efficiently, but in other circumstances it may not allow users who have provided a sustained signal for incremental capacity to obtain all the incremental capacity requested (as volumes may be

pro-rated in aggregate, regardless of the fact that one individual user has provided a sustained signal).

Addressing issues with shipper long term contracting

Nigel Sisman gave a presentation on the issue of end user contracting and the UNC. First Nigel provided an overview of the current regulatory framework and noted that a recurrent theme associated with NTS exit reform has been the inability of gas consumers to contract directly with the transporter. Nigel outlined two potential approaches to address the issue: a revision of the Gas Act (or a new exemption) or a bilateral contract "fix" between gas consumer and a shipper.

Under the first option the Gas Act could be revised to permit direct contracting or an exemption for gas consumers in this area might be granted. However, Nigel noted that the case for these changes would need to be made to the DTI.

Nigel noted that an alternative approach might be to consider a new form of gas consumer – shipper capacity contract. Under this approach a consumer would appoint a shipper as its agent and would tell the shipper how much capacity it wants and when. Then, nearer to the gas flow, the consumer would tell the shipper agent which shipper would be "supplying", and the shipper agent would trade capacity to the supplying shipper. The consumer would pay the agent for capacity holding and a service fee.

Avian Egan asked how overruns would be dealt with under this model. Nigel replied that this is an issue that would need to be addressed. Phil Broom noted that there may be contractual solutions but additional complexity may need to be introduced.

Mike Young suggested that it may be worth investigating whether reservation and use of capacity can be separated under the Gas Act. Eddie Profitt suggested that ARCAs at the moment have a similar role. Mike Young replied that ARCAs are currently signed by the developer and the shipper. Paul Roberts noted that ARCAs do not allow parties to book capacity.

There was some discussion on what the current terms of the ARCA are. Eddie Profitt asked NG NTS to circulate the latest version of the ARCA at the next EOWG.

Action: NG NTS to circulate latest version of ARCA at EOWG 6.

Julie Cox noted that credit issues would be very important under a contractual solution. She noted that the credit guarantee needs to stay with the consumer and noted that the real issue is when the customer goes out of business.

Mike Young noted that the interaction between shipper contracting and capacity reservation needs to be explored in more detail. Participants agreed to discuss this issue at the next EOWG.

Action: Mike Young to present at EOWG 6 on the interaction between shipper contracting and capacity reservation.

Further thinking on the flexibility product

Eddie Profitt noted that, in his view, partial interruption fulfils a similar role to the flexibility product and questioned whether the flexibility product is necessary. Nigel said this was a very unsophisticated way of managing flexibility.

Nigel Sisman briefly summarised the presentation on flexibility that was not done, due to time constraints, in the Gas Offtake Seminar in the morning.

Nigel noted that NG NTS would welcome views on the options for flexibility products that were introduced in previous EOWGs. In particular, Nigel invited participants to consider the implications that different slopes of the transmission/flexibility substitution line on the "expandable" product may have.

Nigel noted that work is being undertaken at NG NTS on the expanding flexibility product and said he would expect two months would be needed to reach an answer on the slope of the transmission / flexibility substitution line.

Asked by Nick Wye, Nigel explained that the graph of the expanding flexibility product presented relates to a single node, and noted that the slope of the transmission/flexibility line would be an approximation. Mick Curtis suggested that products with different slopes of the transmission/flexibility substitution line could be offered by NG NTS at different prices. Nigel noted that there is a trade-off between the effectiveness of the product offered and its complexity. Suzanne Turner added that a short term allocation of flexibility may address users' concerns.

Nick Wye noted that users who are helping the system with their flexibility profile should be credited. Nigel Sisman stated that this could be taken in consideration. Chrissie Skyes noted that a anti-diurnal storage product was first proposed during discussions as part of the TANIF model. Nigel reiterated that it depends on how much complexity users are prepared to accept. Chrissie Skyes noted that the arrangements may recognise different types of users. Nick Wye stated that there may be bilateral arrangements by which NG NTS buys flex from users. Chrissie Skyes stated that she considered that the expandable flexibility model is better than the TANIF model.

Julie Cox asked what other feedback NG NTS wanted from users. She noted that there is a general feeling that the expanding flexibility product is better than the TANIF model, but noted that it is very difficult to obtain the data to undertake any historical analysis. Nick Wye noted that the issue under this proposal is that participants may pay for something they do not need. Jason Mann replied that currently direct connects need to book their peak requirements.

Derek Russell suggested that an alternative product that has merit for further consideration is the "flat and increased tolerance" flexibility product as suggested by NG NTS in a previous presentation with the "expanding" flexibility product bolted onto it.

Nigel Sisman stated that it would be useful if users could think where their flexibility requirements would be if they had to use the proposed products now. Julie Cox noted that some data analysis is required, but explained that data is not available. Nigel Sisman stated that he would be surprised if sophisticated users do not have some understanding of what their within day profile may be. Julie Cox replied that this may be driven by a number of market factors. Julie also noted that understanding the overrun regime would be very important to the assessment of the model. Mick Curtis noted that there may be issues with generation, as they could alter their behaviour in response to the products introduced. Nigel Sisman noted that this kind of discussion would provide valuable insight.

Jason Mann proposed that NG NTS prepare a strawman, assuming a gradient for the transmission/flexibility substitution line (recognising that work still needs to be done on this), and addressing all the other related issues.

Action: NGG to present at EOWG 6 on a strawman of the proposed arrangements for flexibility (including proposed approach for overruns)

Presentation on revenue drivers

Suzanne Turner gave a presentation on revenue drivers. Firstly, Suzie explained that a revenue driver is a revenue allowance that links revenues to an output measure such as capacity provided. Suzie added that it applies to additional capacity above baseline subject to meeting certain criteria.

Suzie noted that Ofgem's initial thinking is that revenue drivers should apply to all load related capex, with static baselines. Suzie explained that this would be a simple approach consistent with a user commitment model.

Suzie also outlined a number of questions that need to be addressed, such as:

- How/when should the revenue driver be triggered?
- What are the prerequisites for the application of the revenue diver? (capacity bookings, delivery of capacity, actual investment undertaken / required)
- At what point should the assumed (in the revenue driver) cost be reconciled with actual costs? Should the reconciliation be retrospective?
- Should there be flexibility for revenue drivers to be disallowed in some circumstances?

Finally, Suzie outlined a number of issues on the form of the revenue driver, such as the spatial definition, or whether it should be indexed / parameterised and vary with capacity increment. Suzie stated that the objective is to keep revenue drivers as simple as possible whilst providing revenue allowance broadly consistent with efficient costs on aggregate.

Suzie noted that Ofgem is keen to receive data from NG NTS to understand where the tradeoffs lie.

Mick Curtis questioned the interaction between revenue drivers and ARCAs. Suzie noted that ARCA are separate from revenue drivers, as they simply represent a commitment to pay charges.

Presentation on buyback

Suzanne Turner did a presentation outlining Ofgem's initial thoughts on buyback. Firstly, Suzie explained the current exit buyback incentive. Suzie then noted that NG NTS may undertake buyback for investment reasons (e.g. late delivery of capacity) or for operational reasons (e.g. planned and unplanned outages).

Suzie outlined a number of issues to be addressed relating to buyback, such as:

- Different drivers,
- Market power at offtake points;
- Managing costs / risk to customers in the event of late delivery of investments;
- Increasingly lengthy planning consents process;

- Interactions with baseline model, interruption regime and emergency arrangements.

Suzie finally outlined some questions specifically related to investment related buybacks (such as whether the price may be set ex ante or if there is scope for flexible contracting) and to operational buy backs (for instance asking whether a price control model may be more appropriate for operational buy backs).

Nick Wye noted that there should be some kind of protection on the customer side as well, as the risks should be equally balanced. Mick Curtis expressed some reservation on the introduction of zero price buy backs.

Next meeting

Robert Hull thanked participants for their contributions. He said that the next EOWG is scheduled for Wednesday 8 March and that, among other things, the following issues will be discussed:

- interaction between shipper contracting and capacity reservation;
- strawman of flexibility product (including overrun issue)
- interruption.