ofgem

Minutes

Gas SCR: Workshop on revised options

This workshop provided a forum to review the high level messages from the responses to the initial consultation and to discuss and gain feedback on the revised options for reform.	From Date and time: Location	Ofgem 1 April 2011; 10am-4pm Broadway House, Tothill Street, London SW1H 9NQ

1. Workshop agenda

1.1. Ofgem introduced the workshop with a presentation[1] on the emerging messages from consultation and revised potential reform options. This was followed by a question and answer session. After this, attendees were divided into two break-out sessions to discuss the reform options in more detail.

1.2. The agenda for the break-out sessions was as follows:

- options for non-daily metered customers
- options for daily metered customers
- options for emergency cash-out arrangements
- options for enhanced obligations
- bundling of options.

1.3. This note provides a high-level summary of the issues discussed and the views expressed by attendees in the break-out sessions in particular.

2. Non-Daily Metered (NDM) customers

2.1. The main focus of this discussion was around the option of providing compensation at the administrative value of lost load (VoLL) for firm NDM customers who have their gas supply interrupted.

2.2. There were some doubts among attendees over whether, in the context of this perceived low risk, shippers or suppliers would invest in measures such as storage if compensation payments for firm NDM disconnection were introduced. A number of shippers suggested that the risks would be insufficient to support a feasible business case for investment, with one storage operator suggesting that new investment would not be forthcoming without the certainty provided by an obligation.

2.3. On the other hand, there were questions raised over what level of compensation would be appropriate, with some participants suggesting that too high a level could effectively enforce inefficient strategic storage.

2.4. In general attendees appeared to be in favour of bounding the circumstances in which compensation would be payable, both in terms of a '1-in-x winter' and a 'n-x' infrastructure standard. This was seen as important in managing credit issues both

[1] http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=18&refer=Markets/WhlMkts/CompandEff/GasSCR/SemWrkShp

before and during an emergency. A force majeure event was generally considered to be an event in which compensation payments from industry would not be appropriate.

2.5. Attendees also appeared generally supportive of capping the total amount of compensation payable per customer (for example, to a cap of £1000 per customer or a number of days of compensation). Again, this was due to the credit implications of having unconstrained compensation liabilities on shippers.

3. Daily Metered (DM) customers

3.1. The options discussed included providing compensation at an administrative VoLL for firm DM customers that are disconnected (to allow for greater incentives on interruptible contracts), and an administered auction to discover the DM demand-side (to deliver specified volumes of interruption).

3.2. Some large customers argued that compensation at VoLL would not incentivise customers to seek interruptible contracts — as they do not want to be commercially interrupted, they would be reluctant to accept anything less than the administrative VoLL in the event. Large customers explained that it is difficult for them to assess the probability, and it is a low priority for most businesses. However if the probability of outage was assessed as being higher, some 'low-hanging fruit' may be revealed. A number of attendees were of the view that standard contracts may be required.

3.3. A distinction was made between 'system interruption' (effectively emergency interruption) and 'commercial interruption' (as per normal business practice). Some customers noted that they would only want to offer interruption if it were only offered as a last resort to avoid going into an emergency (i.e. as a contingency measure).

3.4. On the supplier side, it was argued that the Emergency Curtailment Quantity (ECQ) mechanism already provides some incentive to negotiate interruptible contracts. When challenged, suppliers argued that as the probability of an emergency is so low they would be less inclined to offer DM customers an option charge if interruption were only offered in emergency circumstances.

3.5. Given some of the barriers to interruptible contracts identified, a number of participants expressed a preference for National Grid Gas (NGG) to run an auction for an option plus an exercise fee interruptible regime. This could take place pre-winter, and could include either a price or a volume cap to exclude extremes. However, some attendees raised concerns about whether NGG would be able to run such an auction under current legislation.

4. Emergency cash-out

4.1. The main options discussed included leaving the decision of when the freeze cash-out to the Network Emergency Coordinator (NEC), or allowing cash-out to remain dynamic to stage 4 of an emergency.

4.2. There was general acceptance of the need to have some mechanism for command and control at some point during an emergency, to recognise that the market is 'broken' and for safety to take precedence. However there was some agreement on the merits of keeping cash-out dynamic for longer into an emergency (rather than freezing it at stage 2).

4.3. Some argued that the NEC discretion option may provide less clarity as to when NGG ceases taking market balancing actions.

4.4. There was a suggestion from one shipper that NGG could be sole-buyer of non-domestic gas as a last resort, which was supported by a small supplier. However generally attendees did not consider NGG to be the best equipped to fulfil this role (compared to shippers).

5. Enhanced obligations

5.1. The options that Ofgem presented included an information provision requirement, a storage obligation (once off or throughout winter), a pre-winter proof of supply obligation, and licence breaches for firm disconnection.

5.2. Many attendees did not support enhanced obligations as they tend to go against the grain of the market and may raise barriers to entry.

5.3. Of the specific obligations discussed, many attendees considered that the long-term contracts option would need regular monitoring and may therefore become onerous to monitor and report on. As most gas is purchased at the National Balancing Point (NBP), the requirement to hold long-term contracts could also harm market liquidity. Also, as there may be an option to divert gas under long term contract the security of supply benefit is somewhat unclear.

5.4. A number of attendees considered that a storage obligation at the start of winter could work, but that it would need to specify type of storage (i.e. Long Range Storage) if we wanted to avoid checking levels over the course of the winter. A number of shippers / suppliers noted that it will take some time to build more storage, therefore any obligation would need to ramp up over time. There were concerns expressed by small suppliers at the potential increase in barriers to entry.

5.5. Some attendees suggested that a licence breach if any firm NDM customers were disconnection would be overly onerous and difficult to put into law.

6. Bundling of options

6.1. Many attendees felt that it would be difficult to give a view on an appropriate package without further detail around the proposed options.

6.2. While reiterating its commitment to delivering on the objectives of the Gas SCR, Ofgem emphasised that all options remained on the table and that the Impact Assessment would consider a number of options packages.