

## Gas Transmission Policy Working Group 16<sup>th</sup> January 2019

From: Jon Sharvill

Date: 16<sup>th</sup> Jan 2019

Location: ENA, London

Time: 10:00-17:00

### Present:

Kelvin Hui, Kirsty Earle, Jon Sharvill, Craig Molyneux (ext), Lea Slokar (ext) (*Ofgem*)

John Perkins, Alex Ferguson (*National Grid*)

Julie Cox (*Energy UK*)

Gregory Edwards (*Centrica*)

John Costa (*EDF Energy*)

Lorna Millington (*Cadent*)

Bill Reed (*RWE*)

### Apologies:

None

### Item 1: Introduction

1.1 It was explained that the purpose of the working group was for Ofgem to receive feedback on the Gas Transmission (GT) sector-specific consultation document, and that there will be a further session to discuss the cross-sector elements of the consultation.

### Item 2: Overview of RIIO-GT2 Package

2.1 Ofgem outlined the overview of proposed outputs and incentives for RIIO-T2 and described the output categories and types of output. Stakeholders asked if we could create a similar chart showing which outputs and uncertainty mechanisms are being removed so it is clear which ones will be used in RIIO-T2, to which Ofgem agreed.

2.2. Ofgem stated that where it is offered that stakeholders value a service, the onus will be on NGGT to provide empirical evidence of that value. Stakeholders noted that it is difficult in placing a monetised value on certain outputs, such as customer satisfaction, and it is about behaviour and attitudes rather than economic value. Stakeholders said that defining any potential value should be a joint endeavour between Ofgem (as consumer advocate) and National Grid, noting that Ofgem talked about consumer value in the December Document without quantifying this.

2.3 Ofgem described the different proposed approaches to setting targets, rewards and penalties in RIIO-T2. Stakeholders said that the underlying principles are fine, however it

is difficult to see how and where this applies to GT, especially the use of dynamic and/or relative incentives. Some stakeholders questioned the assumption that year-on-year improvement – a prerequisite for relative absolute schemes) is achievable, and queried Ofgem using ‘ratchet’ schemes that make targets more challenging. It was suggested that using dynamic targets may weaken the ambition of NGGT to outperform targets early in the price control as this would make it harder to achieve rewards beyond that. Stakeholders also noted potential problems with timing and implementation, as Y1 performance is unlikely to be known until mid-way through Y2, so there could be lag effects. Ofgem agreed further thought will be needed on how this could apply to the GT sector.

2.4 Ofgem confirmed that it is open to NGGT proposing bespoke outputs if its stakeholders desire anything additional that was not included in the consultation document, and encouraged early engagement on this.

### **Item 3: Stakeholder Engagement Incentive / Satisfaction Survey**

3.1 Regarding the Satisfaction Survey, Ofgem reiterated that it was aware that there is stakeholder fatigue.

3.2 Stakeholders noted that the surveys are particularly impacted by the “recency” effect, which is especially prevalent in the distribution sector whereby those who are surveyed directly after an event, e.g. connections, provide greatest value in response. However, those surveyed after a prolonged period after an event are prone to provide more generic feedback.

3.3 Some stakeholders also questioned the legitimacy of removing the incentives given stakeholder engagement is increasingly considered BAU, and questioned whether the financial value of the incentive actually stimulates behavioural change.

3.4 Some stakeholders highlighted that they will be holding an engagement event and have invited Ofgem to talk through their proposal.

3.5 Stakeholders also highlighted the transmission system hides responses to upstream constraints; that there is in fact a whole system element that is not captured in the satisfaction surveys.

3.6 Stakeholders noted that the weighting between the engagement and survey incentive is ‘backwards’ and is opposite of what is in the GT sector specific consultation.

3.7 Ofgem again raised the question as to whether or not the two elements can be merged together. Stakeholders responded that merging the two elements may dilute the purpose of the incentive. It was also noted that the satisfaction score seems more important but also that the quantitative element helps focus NGGT’s team and is a useful barometer.

3.8 One stakeholder expressed a view that the value to consumers of good stakeholder engagement was high compared to the size of the incentive.

## **Item 4: Quality of Demand Forecasts**

4.1 Ofgem stated an intention to retain the quality of demand forecasting incentive and asked for views on whether stakeholders see any value in widening the forecasting available to include further data items, and whether wrapping up wider data provision into a single incentive would be appropriate. Stakeholders responded that they are conscious of GT having lots of smaller incentives, but it is difficult to see how they could be rolled into one single incentive. Stakeholders noted that bundling different elements together could make the incentive more complicated, and lead to NGGT focusing more on aspects it knows it can do well. Stakeholders also highlighted potential difficulties in weighing the different elements.

4.2 Stakeholders asked what the impact would be if the incentive was removed and there were no forecasts, as it is not clear exactly what the benefit is. It was said that it could lead to critical pressures being put at risk if the forecasting is wildly wrong, and that the data is used throughout the industry. Stakeholders replied that it should be determined how accurate the forecasts need to be in order to avoid adverse consequences.

4.3 Stakeholders stated that the introduction of smart metering should negate the need for the incentive in the future. The cost of c.£3m a year to provide the forecasting was questioned by some stakeholders, and it was suggested that removing the D2-5 forecasting or trading it for some other information, such as non-daily metered (NDM) data, could be beneficial. In response, it was noted that smaller shippers value the D2-5 forecasting and there were other stakeholders not in attendance that also value the service.

4.4 Some stakeholders suggested that £3m a year was low for the value to the industry and the risk if the incentive was taken away, and also questioned whether the incentive should be weighted towards higher demand days (i.e forecast errors have bigger impacts on high demand/high market price days)

## **Item 5: Maintenance**

5.1 Ofgem asked stakeholders whether the maintenance incentives should be considered BAU or whether there is value in keeping the incentive. Stakeholders said that they do not think it is yet BAU, noting that it took a long time to get this incentive in place and although it has flaws, it is better than not having the incentive and has driven a step-change improvement in how maintenance is managed. Stakeholders noted that the incentive has only been in operation for a relatively short period of time and they do not want to see it removed so quickly, although they are open to tightening the incentive.

5.2 Some stakeholders challenged the option of making the incentive downside-only, stating that this does not take into account the costs involved in meeting the target such as paying staff overtime, and that the incentive must also consider the increased asset health work required in RIIO-T2. Stakeholders noted that the size of the incentive is small relative to the value picked up elsewhere, such as keeping power stations online, and that moving to downside-only may not encourage desired behaviour. Stakeholders also noted that maintenance is a whole system issue, as it also has knock-on effects on the electricity system.

## **Item 6: Connections**

6.1 Ofgem stated its belief that the output has been successful in driving behaviour, and proposed retaining the incentive without modification. Stakeholders asked for clarification of how Project CLoCC affects this incentive, to which Ofgem replied that CLoCC enables NGGT to comply with the output more easily. Stakeholders asked whether there is any benefit of making connections earlier, to which other stakeholders replied that it is possible for smaller customers, but may not be for larger customers. Ofgem agreed that the connection timeframes are an area that can be looked at in the future.

## **Item 7: Constraint Management**

7.1 Ofgem proposed tightening the incentive and invited views on the balance of risk versus the size of the reward/penalty. Stakeholders highlighted the opaqueness of the target setting process, to which Ofgem replied that the targets will be influenced by the capability review and that the process needs to be transparent. Stakeholders noted that the current scheme is based around low probability high impact events, and using a small historical dataset might not be appropriate in gauging future performance. Stakeholders suggested that the low probability high impact aspect could be replaced with an alternative mechanism. It was noted that the size of the incentive is very large relative to other incentives, and given the lack of network constraint and high baselines, the sum of money seems too large. This was acknowledged, with the caveat that five years of outperformance could hypothetically be wiped out in one bad week. It was then discussed who should bear the risk of a very bad week.

7.2 Stakeholders stated that it was not clear how the targets in RIIO-T1 had been determined, and that industry either needs more transparency from NGGT or Ofgem need to take up the role and find the appropriate balance between risk and reward. Ofgem agreed that it wishes to see more transparency in how NGGT minimises the impact of low probability high impact events.

7.3 Stakeholders asked whether it could be beneficial to separate the pre-planning for low probability high impact events and the remedy. Ofgem raised the possibility of providing baseline expenditure for preventative action.

7.4 Stakeholders asked what the difference is between TO constraints and SO constraints, as the cost drivers are different. It was said that SO constraints are more relevant to the electricity sector than gas, and it was not clear that there should be a distinction. It was agreed that many elements feed into the incentive and Ofgem agreed to send a note to stakeholders detailing exactly what feeds into the model.

7.5 Stakeholders acknowledged that this incentive is linked to the capability assessment, noting that if baselines are high then the incentive should be retained in a similar form, while if baselines are low there is less need for the incentive, and targets should be recalibrated accordingly.

## **Item 8: Residual Balancing**

8.1 Ofgem stated its proposal to retain the incentive but tighten it in RIIO-T2. Stakeholders disagreed with Ofgem's statement in the sector-specific consultation document that the purpose of the incentive is to minimise reaction in the market, stating instead that the purpose is instead to cause a reaction in the market, which Ofgem acknowledged.

8.2 Stakeholders suggested that linepack is an area that should be explored during the building of NGGT's business plan. Some stakeholders felt the incentive disproportionate as for the majority of the time NGGT's actions are BAU. Other stakeholders said that the system would still operate efficiently without the linepack incentive, that the incentive did not work when it was most required during 2018's 'Beast from the East' extreme weather period, and that NGGT win most of the time from this incentive.

8.3 There was a discussion about how robust the incentive is in situations where linepack is used differently. It was agreed that the design should be looked at, as just using start of day/end of day levels may not be the most appropriate measure. Stakeholders recognised that there are issues with weekend versus weekday and summer versus winter demand, which is not currently reflected in the incentive mechanism, and raised the possibility of adding a weighting to the incentive for when it is more/less important.

8.4 Stakeholders recognised that the incentive is important both to NGGT's control room and to wider industry, that NGGT's behaviour has changed in response to the incentive, and the size of the incentive is relatively small.

## **Item 9: Network Capability**

9.1 Ofgem explained its rationale for requesting a capability assessment and obligated baseline capacity report, in order to understand how network capability is affected by changing demand and flows, and to align obligated capacities with physical capabilities of the network. Stakeholders stated that they agree with the approach in principle, but highlighted a number of concerns.

9.2 Stakeholder noted that the process is very complicated, and that little will be gained from using a single figure for capability as it does not account for a number of variables that affect the figure at different times of the year. Stakeholders said that giving figures for maximum flow at each entry and exit point will give a huge number that is not reflective of how the network can operate, and it may be better to give a range of capabilities given certain sets of assumptions.

9.3 Stakeholders said that while substitution has been recognised as a good method of alleviating system constraint, if baselines are lowered this lessens the likelihood of substitution being possible. It was also stated that there are many system interlinkages that influence network capability, and caution should be exercised in interpreting the data and determining what the outcome should be.

9.4 Stakeholders said that customers do not want to see capabilities reduced, and lowering baselines may lead to pressures being reduced. Ofgem accepted that pressures are something that needs to be looked at, and highlighted the need to understand what the efficient capability of the network is, as it is currently difficult to see whether investments have been efficient.

9.5 Stakeholders stated that NGGT are not planning to put in pipelines in RIIO-T2, and are not intending to remove any until a further needs case arises, and enquired where the data on the network will be used by Ofgem. Ofgem replied that it will help assess the needs case for investment.

9.6 Stakeholders acknowledged that the idea of a capability report is good, but queried the terms of reference of the document and what Ofgem see coming from it, noting that it may worry industry who will have to prepare for and contribute to the report. It was

also suggested that the capability ranges will be so great that it will be difficult to draw meaningful information. Ofgem responded that it will be useful when thinking about multi-compressor, multi-system investments as it will be useful being able to tie operating ranges to investments.

9.7 Stakeholders asked if the focus is more on entry or exit. It was stated that the focus is on the network as a whole, with no priority between entry and exit.

## **Item 10: Access Arrangements**

10.1 Ofgem acknowledged that since substitution was introduced lots of successful arrangements have dealt with capacity without cost to consumers, but still see room for improvement. Ofgem noted that much of what is being proposed is already happening elsewhere and invited views on whether zonal access arrangements should be considered.

10.2 Stakeholders asked what was meant by zonal capacity substitution, and whether there will be zonal exit capacity products. Ofgem replied that the current system is on a nodal basis, and asked NGGT to explore having a zone where a request within the zone would be dealt with from within the pool of capacities within that zone. Ofgem stated that having zonal exit capacity products is a possibility.

10.3 Stakeholders recognised the challenge of determining how zones are defined and what exchange rate should be used. It was also noted that it would take several years to transition from a nodal to zonal system, and it will be difficult to prepare for this in time for NGGT's business plan deadlines. Ofgem responded that the intention was only to make the idea public, then further discussions can follow around what is and is not implementable. Stakeholders recommended taking a comprehensive approach to this so industry knows the direction of travel, and stated that it needs to be done in the context of baselines, substitutions, and the system being fit for purpose. Stakeholders said that they would like to see a plan or framework from NGGT even if it cannot be implemented before the start of RIIO-T2.

10.4 Stakeholders acknowledged there were elements of access that could be reviewed, with scope for improvement. However, the potential scope of topics could be wide and require substantial time to complete fully. As the outcomes are highly unlikely to impact NGGT's RIIO-T2 business plan it was questioned why a review was not part of normal industry changes processes and why Ofgem had linked the RIIO business plan and related timescales.

## **Item 11: Cyber and Physical Security**

11.1 Ofgem proposed that NGGT submit a strategic investment plan in line with Ofgem and BEIS' direction as the competent authorities on cyber resilience, and expect to see this in the business plan. This was acknowledged by stakeholders, who consider cyber and physical security to be BAU items.

## **Item 12: Compressor Emissions**

12.1 Ofgem proposed a long-term emissions compliance strategy from NGGT and consulted on how price control deliverables (PCDs) should be set. Stakeholders highlighted issues concerning timelines and the practicalities of setting PCDs based on

information in a December 2019 business plan. It was noted that a full BAT assessment process will not have been completed in time for the submission of NGGT's business plan. Stakeholders also said that a single re-opener in RIIO-T2 means that, if with hindsight PCDs are set incorrectly, it could introduce delays until the 2023 reopener. This delay would shorten the time available to achieve compliance across the whole compressor fleet by the 1<sup>st</sup> January 2030 deadline.

12.2 Stakeholders said that the compressor compliance programme is BAU and has to be delivered to achieve compliance, and questioned why it is being incentivised. Ofgem responded that the intention is more to make it clearer exactly what is required from NGGT.

12.3 Stakeholders said that using PCDs may dampen the use of innovation, and setting PCDs based on the December 2019 business plan might not offer sufficient flexibility. Stakeholders added that compressors play an important role in system flexibility and highlighted the distinction between the operability and investment aspects of the output, so NGGT's plans must focus on both IED compliance and system operability. Stakeholders noted that the reopener for compressor investment should not be restricted to achieving environmental compliance and should consider that some compressor investment may be linked to delivering stakeholder requirements from the network.

12.4 Ofgem recognised the challenges posed by compliance in terms of capability and operability and agreed to take stakeholder views on board and consider the next steps. Ofgem agreed to prioritise updating stakeholders with guidance on system capability/operability following further internal discussions. Ofgem agreed to attend a meeting with Energy UK to discuss the issue further.

## **Item 13: Greenhouse Gas Emissions / Venting**

13.1 Ofgem stated the proposal to roll the incentive over into RIIO-T2. Stakeholders questioned why the scheme is downside only when other networks have an upside component. Ofgem replied that on principle it is against rewarding NGGT for emitting any level of greenhouse gas.

13.2 Stakeholders suggested that the incentive could be widened in scope to include other elements, such as venting from pipes. Ofgem responded that it is open to this.

13.3 Some stakeholders said that the reputational aspect may be sufficient to encourage desired behaviour, and others questioned whether the incentive could be incorporated as part of the shrinkage incentive. Ofgem asked how removal of the incentive would affect NGGT behaviour, to which stakeholders replied that there it could mean leaving compressors on standby for longer than would otherwise be the case rather than venting gas.

## **Item 14: NTS Shrinkage**

14.1 Stakeholders noted that NGGT manage to consistently outperform its target, and asked whether there were any calibration issues and whether the formula is set correctly. Stakeholders also said that the size of any reward/penalty should be related to the cost of carbon, the cost of the impact and the level of emissions. Stakeholders also asked whether the current scheme provides value for money versus the cost saving.

## **Item 15: BCF Reporting and Low Carbon Energy Systems and Decarbonisation of Heat**

15.1 Some stakeholders questioned why this is being incentivised by Ofgem rather than the government, noting that NGGT are a facilitator rather than a player. Ofgem stated that this is a whole systems approach, and it was important to see what steps are being taken within the gas transmission sector. Ofgem agreed to provide further clarity on what is required on NGGT's plan to support the low carbon transition.

## **Item 16: Uncertainty Mechanisms**

16.1 Ofgem invited views on removing the uncertainty mechanisms highlighted in the consultation document. Some stakeholders stated that they did not see the logic in removing one off asset health shocks just because they were not necessary in RIIO-T1, as this does not mean they will not be required in RIIO-T2.

16.2 Stakeholders highlighted removal of the network flexibility uncertainty mechanism and the ability to accommodate changing flows on the network. It was suggested if something happens, for example, to make flow rates from Norway collapse, something needs to either be built into the price control or be kept as an uncertainty mechanism with a threshold trigger. Some stakeholders also suggested retaining the quarry and loss mechanism with a threshold trigger.

## **Item 17: Any Other Business**

17.1 None

## **Item 18: Next Steps**

18.1 Stakeholders to respond to the consultation document by March the 14<sup>th</sup>, with the aim to publish responses by mid-May.

18.2 Noting difficulties knowing which areas of the consultation document require the most considered responses, Ofgem will inform stakeholders of the main priorities for receiving feedback at the earliest opportunity.

18.3 Ofgem will provide stakeholders with guidance on system capability and operability, as per section 12.4

18.4 Ofgem will update the list of incentive proposals, output categories and type of incentives to reflect the outputs that are not being retained in RIIO-T2

18.4 Ofgem will inform stakeholders exactly what elements feed into the capacity constraint incentive model, as per section 7.4

18.5 Next Cost Assessment Working Group is on 22<sup>nd</sup> January. No further Policy Working Groups currently scheduled.