Distribution Charging Methodology Forum

Minutes

Thursday 24 May 2007

Elexon Offices, 350 Euston Road, London

Attendees

Tim Davis (Chair)	TD	Joint Office of Gas Transporters
Lorna Dupont (Secretary)	LD	Joint Office of Gas Transporters
Alison Lim	AL	Shell Gas Direct
Anna Taylor	AT	Northern Gas Networks
David Jessop	DJ	Scottish and Southern Energy
Denis Aitchison	DA	Scotia Gas Networks
Dennis Timmins	DT	RWE npower
Eddie Proffitt	EP	MEUC
Fiona Upton	FU	E.ON UK
Gareth Davies	GD	Chemical Industries Association
Graham Craig	GC	Ofgem
James Dumbelton	JD	Shell Gas Direct
John Edwards	JE	Wales & West Utilities
John McNamara	JM	Ofgem
Lorraine Goodall	LG	Scotia Gas Networks
Lisa Waters	LW	WatersWye (for Corona Energy)
Phil Broom	PB	Gaz de France
Rochelle Hudson	RH	Centrica
Sandra Spence	SS	ScottishPower
Stephen Marland	SM	National Grid Distribution
Steve Armstrong	SA	National Grid Distribution
Sundeep Klair	SK	Energy Networks Association

1. Introduction

TD gave an introduction and explained the purpose and focus of the meeting.

1.1 Minutes of Previous Forum

The minutes of the forum held on 19 April 2007 were accepted.

1.2 Actions

0003: JO to inform Users of consultation timescales and website location of discussion paper.

TD informed the forum that this action had been completed. **Action Closed**

0004: Ofgem to investigate the background to the decision on the original 50/50 split and the ensuing developments that had led it to conclude that this was no longer appropriate.

Ofgem explained to the forum that the decision to reject 90/10 in favour of 50/50 was a conclusion reached based on the best available information at the time (1996). There had been a great deal of change subsequently, and the information now available supported a different conclusion. **Action Closed**

0005: DNs to prepare cost breakdown information to clarify the fixed/variable cost element underlying the proposed capacity/commodity split.

This was addressed within the presentation. **Action closed**

0006: DNs to develop and present typical scenarios that demonstrate the effect of the proposed change on charge cycling.

This was addressed within the presentation. **Action closed**

0007: Statoil to consult with interruptible customers for their views on the impact of the proposed change.

Statoil did not attend this meeting. **Action carried forward**

0008: DNs to produce impact by load band for each DN to reflect analysis already presented for the Southern DN

This was addressed within the presentation. **Action closed**

2. Presentation and Discussion

2.1 PDDN02: LDZ System Charges Capacity/Commodity Split and Interruptible Discounts

2.1.1 Summary of responses received

DA presented a draft summary of the responses received and advised that a full report containing the DNs' responses to the points raised would be produced shortly.

Discussions took place relating to each of the sections.

1 Should the Charging Methodology be changed so that the capacity element of the LDZ system charges is set to recover around 95% of the revenue from the LDZ system charges for all DNs.

DA advised that several Shippers had concerns about the impact of the proposal on domestic customers and the fuel poor. This was expected to be 1% on transportation charges.

Shippers had also argued that small domestic users would be disadvantaged by more capacity charges with a disproportionate effect on those in fuel poverty, and that there was a concern that the proposal passed on an increased cash flow risk to Shippers/Suppliers. However, the DNs did not think there would be a significant effect in either case.

SM stated that 65% of capacity charges were already fixed. SS countered that there were customers who did not have any fixed charges. LW and SS agreed that charges did not have to reflect the DNs price structure. SA observed that previous changes in the capacity commodity split had not provoked new domestic tariffs. SA suggested that only about 6% of the end-user cost was involved, to which LW responded that such "small" percentages were significant for Shippers and Suppliers.

2 Should the change be made with effect from 1 April 2008.

There was a discussion on the merits of price changes in April or October.

The DNs thought it advantageous to the community to know what the structure of charges would be before participation in the interruptible auctions. It was thought that some interruptible consumers may want to review, and reduce if appropriate, their SOQs.

EP observed that a significant number of consumers would be renewing their contracts in October, and would therefore be making decisions based on 50% of known information and 50% unknown with an April change. PB confirmed that 50% of I & C contracts were likely to be renewed in October and that there may be a temporary shift or 'pain' if an April change in charges was anticipated. AT thought that that a certain degree of detail may be able to be provided to assist in managing this.

SS and LW preferred to see the time of any change shifted to a later date as there was a long lead team in negotiating contracts. EP suggested looking at implementation one year after approval by Ofgem, so that most contracts would be cleared out and the new arrangements could be reflected in negotiations.

DJ asked whether an April date would be more or less stabilising as an adjustment was being made to the capacity/commodity split, not to revenue?

The DNs agreed to consider the points made and reflect them in their final proposal.

3 Should interruptible customers pay a proportion of the increased LDZ capacity charge such that their effective discount on total LDZ firm charges maintains the status quo.

The DNs felt it was reasonably cost effective to levy a share of the capacity charge. Certain fixed costs were related to the running of the Networks and not to capacity; others were variable. The DNs were trying to maintain the current level of discount for the new regime. It was not a long term solution because the whole interruption regime is going to change.

4 Are there any other elements that the DNs should consider in their review of the LDZ system charges split between capacity and commodity elements.

Concerns were expressed about the stability of charges, for example as the level of allowed revenue changed. It was stated that the GDPCR was not targeted at improving price stability, which this proposal was. It was confirmed that the capacity / commodity elements of the NTS charges were still unknown, creating uncertainty.

SS thought that RbD and reallocation to the domestic industry was at an unacceptable level and could see RbD going up because of the proposed changes in charging structure. DA, however, thought the volume to be reconciled would go down. DJ questioned how the imbalance between AQs in the domestic and small business market would be addressed, as the SOQ would now drive 90% of Shipper charges. SM observed that the cap was not reconciled for commodity charges, but EP commented that commodity will be 5% in the future, which was a tiny percentage.

DJ reiterated that the AQ drives the SOQ. How would this proposed change better allocate costs as the AQ is not accurate even now? RbD addresses an imbalance from domestic to business customer. AQs were already mismatched, and if there were an issue with the AQ the SOQ would also be affected. Was there an intention to move away from AQs and RbD by changing charges?

SA confirmed there would be RbD in the future, and LG agreed that the DNs needed to think through this area and elucidate at the next meeting.

Action 0009: SS and DJ to specify concerns regarding the impact of the capacity commodity split change on RbD for the DNs to consider.

5 Other issues/questions raised

The DNs commented on the following points raised:

- **What effect would the proposal have on payments made to DN Interruptible customers in the event that they are interrupted for greater than 15 days?**

  DA stated the DNs do not see this as changing. LW thought that this was something for Ofgem to consider; whether there is something that could be offered to I&C customers in terms of compensation payments, or fines if the networks fail to deliver gas. It was accepted that this was not a charging methodology issue but could be addressed as part of the GDPCR. EP suggested that there should be no capacity charge if it was not available on a particular day, akin to ratchet charges in reverse.

- **Is the capacity/commodity split likely to change over time and if so, when should the split be reviewed.**

  DA commented that there was an obligation to keep the charging methodology under review but that it was not expected to move in the near future.

  EP suggested using the electricity system as a model, where capacity was booked and paid for whether it was used or not – this would present a visible fixed charge. DA responded that the DNs were trying to be cost reflective and that electricity had a different cost base. EP observed that it did not change on an annual basis, and suggested simplification by scrapping RbD and AQs and generating charges purely on booked capacity. SA did not think that would be as cost reflective as the current proposal.

2.1.2 DN Cost Information

Impact on stability of charges

Impact analysis by load band

SA gave a presentation covering these issues.

PB asked whether the variation in commodity related costs (5% and 4%) meant there was a possibility that the DN charging methodologies could diverge. Shippers confirmed they would not want to see a diverging charging structure. JMc stated that Ofgem recognised the trade off between cost reflective and facilitating competition through a common methodology.

In response to a question on scaling from DJ, DA and SA advised that cost analysis was used to determine the structure of charges, whereas allowed revenue, volumes etc were used to determine the level of charges. AT commented that if volumes increased massively the DNs' costs would not increase.

A range of potential price changes was outlined which reflected differing times from moving to 95:5 and a range of potential GDPCR outcomes. GC thought that it was most important to concentrate on longer term stability as it was important to consider the whole price control period rather than just the next 6 months.

TD observed that there appeared to be unanimous opposition from Shippers to the April 2008 change, but the question remained as to whether October 2008 or April 2009 was preferred.

EP wondered if the change in methodology could be established for October 2007, such that the effect of the price control would be seen as it stands alone.

SA suggested April 2009 would have the benefit of the price control outcome being known. LW thought that this would give more opportunity to change contracts, talk to customers, etc and would prefer the longer lead time. SA observed that there would be exposure to under/over recovery in the preceding winter to April 2009. If the change was made earlier this would be avoided, and October 2008 may be a compromise position.

LW stated that the charges were not passed through to customers, but were absorbed by the Shippers/Suppliers. This feeds into the domestic arena. More time would give the opportunity to adapt, as domestic prices do not change very quickly. GC thought that a proposal could be made and decided in the summer.

EP observed that I & C charges can be passed through. SS responded that domestic prices drive consumer behaviour; regardless of throughput, it will be behind the daily charge because of the usual current domestic methodology.

SM asked whether Suppliers were seriously thinking of introducing standing charges for domestic customers, but received no commitment.

DJ commented that more stability and predictability year on year, with small changes, would help improve public relations; the domestic message would be more unit based and less capacity based, and there was a need to get rid of volatility in transportation charges. AT commented that removing the weather effect on price charges would mean a closer alignment to allowed revenue, which would make for more stability and predictability.

SA advised that the consultation report would be produced in early June, the consultation paper in July, followed by the final proposals, which would then go to Ofgem. GC confirmed that that Ofgem was expecting the proposals and did not think a new Impact Assessment would be necessary – Ofgem was in the process of updating its earlier Impact Assessment.

2.2 October 2007 Indicative Charges

Discussion of the price changes planned for October 2007 focussed on London. SA stated that while this showed a very large percentage increase, this was bringing the charges up to a similar level to that of the other Networks.

3. Next Meeting

It was agreed that the next meeting would be held in July at a Midlands venue. Details will be confirmed nearer the time.

Action Table (Appendix 1)

Action Ref	Meeting Date	Minute Ref	Action	Owner	Status Update
0001	10/10/06	2.2	SA to send out note extending the deadline for responses to end of week. (JO to receive responses.)	SA	This has been completed **Closed**
0002	10/10/06	3	DNs to consider how DNs will pass-through NTS charges	SA	DNs identified that this consideration would form part of future consultations. **Closed**
0003	19/04/07	2.1	JO to inform Users of consultation timescales and website location of discussion paper.	TD	**Closed**
0004	19/04/07	2.1	Ofgem to investigate the background to the decision on the original 50/50 split and the ensuing developments that had led it to conclude that this was no longer appropriate.	JM	**Closed**
0005	19/04/07	2.1	DNs to prepare cost breakdown information to clarify the fixed/variable cost element underlying the proposed capacity/commodity split.	All DNs	Addressed under the presentation. **Closed**
0006	19/04/07	2.1	Develop and present typical scenarios that demonstrate the effect of the proposed change on charge cycling.	All DNs	Addressed under the presentation. **Closed**
0007	19/04/07	2.1	Statoil to consult with interruptible customers for their views on the impact of the proposed change.	RS	Statoil not present – Update to next meeting. **Carried forward**
0008	19/04/07	2.1	DNs to produce impact by load band data for each DN to reflect analysis already presented for the Southern DN	All DNs	Addressed under the presentation. **Closed**
0009	24/05/07	2.1	SS and DJ to specify concerns regarding the impact of the capacity commodity split change on RbD for the DNs to consider.	Scottish Power (SS) and SSE (DJ)	