










UNC Workgroup Report		At what stage is this document in the process?
<h1>UNC 0605S:</h1> <h2>Amendments to TPD Section K - Additional Methods to Procure and Dispose of Operating Margins Gas</h2>		<div>01 Modification</div> <div>02 Workgroup Report</div> <div>03 Draft Modification Report</div> <div>04 Final Modification Report</div>
<p><b>Purpose of Modification:</b></p> <p>This modification seeks to enable National Grid NTS to procure and dispose of Operating Margins Gas in a more efficient and economical way.</p>		
	<p>The Workgroup recommends that this modification should:</p> <ul style="list-style-type: none"> <li>be subject to self-governance procedures.</li> <li>issued to consultation.</li> </ul> <p>The Panel will consider this Workgroup Report on <b>20 July 2017</b>. The Panel will consider the recommendations and determine the appropriate next steps.</p>	
	High Impact: None	
	Medium Impact: None	
	Low Impact: Shippers and National Grid NTS	

Contents		 Any questions?
1	Summary	3
2	Governance	3
3	Why Change?	4
4	Code Specific Matters	5
5	Solution	5
6	Impacts & Other Considerations	5
7	Relevant Objectives	10
8	Implementation	10
9	Legal Text	11
10	Recommendations	13
Timetable		 0121 288 2107
<b>Modification timetable:</b>		Proposer: <b>Debbie Brace</b> <b>National Grid NTS</b>
Initial consideration by Workgroup	05 January 2017	 <a href="mailto:enquiries@gasgovernance.co.uk">enquiries@gasgovernance.co.uk</a>
Amended Modification considered by Workgroup	04 May 2017	 <a href="mailto:deborah.brace@nationalgrid.com">deborah.brace@nationalgrid.com</a>
Workgroup Report presented to Panel	20 July 2017	 01926 653233
Draft Modification Report issued for consultation	20 July 2017	Transporter: <b>National Grid NTS</b>
Consultation Close-out for representations	10 August 2017	
Final Modification Report available for Panel	11 August 2017	
Modification Panel decision	17 August 2017	

# 1 Summary

## What

The UNC currently prescribes that National Grid NTS should run annual tenders in order to purchase and dispose of Operating Margins Gas, which has not changed since the inception of Code. This modification proposes to enable National Grid NTS to use other trading mechanisms in addition to tenders.

## Why

UNC TPD Section K Operating Margins was based on the prevailing market conditions when the code was created 20 years ago and no longer reflects the current climate. There have been a number of changes to the market conditions such that the number of tenders received has reduced significantly as has the use of Operating Margins Gas. The process has been to accept, tender bids/offers in price order irrespective of whether more competitive prices could be achieved by trading through other routes e.g. Over The Counter (OTC) or exchange. It is not economic or efficient to limit the way in which the Operating Margins Gas is procured or disposed of. National Grid NTS is obligated under its licence, Special Condition 8C.2, to procure its Operating Margins requirements in an efficient manner. This Modification seeks to enable National Grid NTS to procure and dispose of Operating Margins Gas in a more efficient and economical way.

## How

In future National Grid NTS proposes it will look to achieve the best price for procuring and disposing of Operating Margins Gas by having the ability to utilise a range of trading mechanisms which are the Over the Counter (OTC), brokered markets and trading exchanges e.g. ICE Endex in addition to tenders. New rules will be introduced to deal with the potential for trading error by National Grid NTS. It will also provide the ability to procure and dispose of gas prior to the end of the Storage Year, as well as at the beginning of the next Storage Year. There will be amendments to conditions within UNC TPD Section K, to facilitate the change in process.

# 2 Governance

## Justification for Urgency, Authority Direction or Self-Governance

Panel determined the modification is unlikely to have a material effect on competition in the shipping, transportation or supply of gas conveyed through pipes or any commercial activities connected with the shipping, transportation or supply of gas conveyed, because this modification is seeking change the process that may result in a minor reduction in costs for Shippers (up to £90k per annum) and an update to the process to be more reflective of the current market.

Modification 0605S will therefore follow self-governance procedures.

## Fast Track Self-Governance Criteria

This modification is not suitable for Fast Track Self-Governance as it is not properly a housekeeping modification required as a result of some error or factual change.

## Requested Next Steps

This modification should: *(delete as appropriate)*

- be subject to self-governance

- issued to consultation

Workgroup participants agreed that this modification is sufficiently developed to be issued to consultation and that it should follow self-governance procedures for the reasons set out above.

### 3 Why Change?

National Grid NTS purchases Operating Margins (OM) on an annual basis in line with both UNC Section K and obligations described in the National Grid Gas Safety Case in respect of the NTS (the Safety Case). The Safety Case places an obligation on National Grid Gas to maintain OM at levels and locations determined throughout the year.

The OM service is used to maintain system pressures in the period before other system management services become effective (e.g. national or locational balancing actions). A further quantity of OM is also procured to manage the orderly run-down of the system in the event of a Network Gas Supply Emergency.

Where National Grid NTS contracts for Operating Margins Capacity at a gas storage facility, National Grid NTS must purchase gas for injection or transfer into the facility. The Operating Margins requirements at each Operating Margins Facility vary over time resulting in the need to procure additional Operating Margins Gas, dispose of surplus Operating Margins Gas or transfer Operating Margins Gas between different Operating Margins Facilities.

When Operating Margins are utilised, the result is a withdrawal of Operating Margins Gas at an Operating Margins Facility and need to refill the Operating Margins Facility, in preparation for a future Operating Margins event.

Such activities to procure, dispose and transfer Operating Margins Gas are often referred to as “reprofiling”.

UNC TPD Section K Operating Margins was originally based on the prevailing market conditions when the code was created 20 years ago, and no longer reflects the current climate. There have been a number of changes to the market conditions such that the number of tenders received has reduced significantly as has the use of Operating Margins Gas. The current process within UNC TPD Section K limits the method to tenders only that can be used to procure or dispose of gas. Tender bids / offers must be accepted in price order, irrespective of whether more competitive prices could be achieved by trading through other routes e.g. via Over the Counter (OTC) or by using an exchange.

#### **What the drivers are and which parties are impacted**

This Modification seeks to enable National Grid NTS to improve the process to procure and dispose of gas in a more efficient and economical way. The drivers for changing UNC to allow National Grid NTS to use other ways of procuring or selling gas are:

- Process is limited by UNC prescribing that only tenders should be used;
- Less competitive prices offered through tenders versus other options (OTC or exchange) and a reduction in the number of tenders received;
- National Grid NTS licence directs that it operate in an efficient and economical way;
- Benefit to shippers of approximately £30k to £90k per annum which feeds through into the Closing Margins Adjustment Charge (UNC TPD Section K 4.4.5);

The Modification has no impacts on either National Grid NTS or Xoserve systems and the effects on National Grid NTS processes and procedures are negligible.

## What the effects are should the change not be made

The Modification provides an improved method to manage the process for the procurement and disposal of Operating Margins Gas. Although, this Modification has a low impact it would benefit as a slightly more economical and efficient operation of the market.

## 4 Code Specific Matters

### Reference Documents

[http://www.gasgovernance.co.uk/sites/default/files/TPD%20Section%20K%20-%20Operating%20Margins\\_4.pdf](http://www.gasgovernance.co.uk/sites/default/files/TPD%20Section%20K%20-%20Operating%20Margins_4.pdf)

### Knowledge/Skills

No additional skills or knowledge is required to assess this modification.

## 5 Solution

It is proposed that a change to Code is made to allow National Grid NTS to utilise other methods to procure and dispose of Operating Margins Gas at its own discretion, such as the OTC, brokered markets or trading exchanges. It is also proposed such procurement and disposal of Operating Margins gas be allowed prior to the end of the Storage Year (before the capacity rights reduce or expire) as well as at the beginning of the next Storage Year.

In order to allow National Grid NTS to procure and dispose of gas outside the tender process, amendments are required to UNC TPD Section K Operating Margins conditions:

- 3.3.7 Existing paragraph removed to facilitate changes to the Operating Margins Gas process;
- 3.3.8 Renumbered as 3.3.7 and circular reference to 3.3.7 deleted;
- 3.7.2 (a) to (f) renumbered as 3.7.3 (a) to (f). The new paragraph provides the ability to procure and dispose of Operating Margins Gas by other methods and before the end of the Storage Year;
- 3.7.2 (g) and (h) removed and new 3.7.3. (g) and (h) inserted to facilitate the changes to Operating Margins Gas and allow National Grid NTS to utilise other ways to procure and dispose of Operating Margins Gas:
- 3.7.3 Renumbered as 3.7.4;
- 3.7.4 Deleted, as the new 3.7.3 (h) and the new 3.7.5 describe the process for dealing with Residual Gas Transfers;
- 3.7.5 Renumbered as 3.7.6 and amended to allow Residual Gas Transfers to be conducted other means; and
- 3.7.6. Renumbered as 3.7.7

Recognising that Operating Margins gas costs are recovered from Users, it is further proposed to include the following rules in UNC TPD Section K to address errors that may occur in the trading activities undertaken by National Grid NTS for Operating Margins purposes.

### Definition

1. An “**Operating Margins Trading Error**” occurs where, in respect of a trade for Operating Margins gas procurement or disposal (executed by National Grid NTS) it is identified by National Grid NTS *ex post* that one or more of the following elements of the transaction were not consistent with intention of the National Grid NTS representative executing the trade:
  - 1.1 The trade **gas price** is different to that which the National Grid NTS representative intended to be the gas price for the applicable trade; or
  - 1.2 The trade **gas volume** is different to that which the National Grid NTS representative intended to be the gas volume for the applicable trade; or
  - 1.3 The relevant trade **date** (or **range of dates**) is different to that which the National Grid NTS representative intended to be the relevant date (or range of dates) for the applicable trade.

#### **National Grid NTS Obligations in the Event of an Error**

2. Where National Grid NTS has identified the occurrence of an Operating Margins Trading Error, as soon as reasonably practicable it will seek cancellation of the relevant trade, or revision or correction of the executed Trade Parameters, to the extent permitted under the relevant Trading System Operator terms and/or policies and/or as agreed by the trading counterparty.
3. Where the actions described in paragraph 2 are not possible, National Grid NTS will undertake trading activity to limit the value of, or rectify, the error.
4. Where further to paragraph 2 the Trading System Operator and/or trading counterparty (as appropriate) permits:
  - 4.1 cancellation of the trade, or revision of all the executed Trade Parameters equal to those intended by National Grid NTS, no Error Value Determination will be made in accordance with paragraph 5 or 6, nor any adjustment made in accordance with paragraph 8 or 9; or
  - 4.2 revision of the executed Trade Parameters, but nonetheless to values *not* equal to those intended by National Grid NTS, the revised Trade Parameters will constitute amended executed Trade Parameters.

#### **Error Value Determination**

5. Where the Operating Margins Trading Error is attributable to the circumstances identified in paragraph 1.1, the value of the error is the difference between:
  - 5.1 the intended gas price multiplied by the executed gas volume; and
  - 5.2 the executed gas price multiplied by the executed gas volume.
6. Where the Operating Margins Trading Error is attributable to the circumstances identified in paragraphs 1.2 or 1.3, the value of the error is the difference between:
  - 6.1 The intended revenue/cost (determined on the basis of the intended Trade Parameters); and

6.2 The net revenue/cost from the trading activities (determined on the basis of the executed Trade Parameters) following any action taken in line with paragraph 3.

### **Adjustment Mechanism**

7. Where the value of the error determined in accordance with paragraph 5 or 6 is less than £50,000 (per occurrence), no adjustments (described in paragraphs 8 and 9) will be made.
8. In respect of Operating Margins gas procurement, for the purposes of the determination of Operating Margins WACOG (as defined in UNC TPD K4.2.1) the intended Trade Parameters will be applied (subject to an absolute cost cap in respect of each Storage Year of £1,000,000).
9. In respect of Operating Margins gas disposal, where
  - 9.1 the value determined in accordance with paragraph 5.1 exceeds the value determined in accordance with paragraph 5.2, or the value determined in accordance with paragraph 6.1 exceeds the value determined in accordance with paragraph 6.2, the Closing Margins Adjustment Charge (calculated as per UNC TPD K4.4.5) shall be decreased by the aggregate value of any such errors occurring within the Storage Year;
  - 9.2 the value determined in accordance with paragraph 5.1 is less than the value determined in accordance with paragraph 5.2, or the value determined in accordance with paragraph 6.1 is less than the value determined in accordance with paragraph 6.2, the Closing Margins Adjustment Charge (calculated as per UNC TPD K4.4.5) shall be increased by the aggregate value of any such errors occurring within the Storage Year; and
10. Adjustments to the Closing Margins Adjustments Charge in any Storage Year will be subject to a cap of £1,000,000 (in terms of absolute costs, i.e. regardless of whether the value increases or decreases the Closing Margins Adjustment Charge).

### **Reporting**

11. National Grid NTS will detail any Operating Margins Trading Errors (that are identified within the Formula Year) within its annual Procurement Guidelines Report (published in accordance with Special Condition 8A of the National Grid NTS Gas Transporter Licence).
12. In respect of each Operating Margins Trading Error detailed in accordance with paragraph 11, the following information will be provided:
  - 12.1 Trading System;
  - 12.2 Trade Execution Time and Date;
  - 12.3 Operating Margins Trading Error Identification Date;
  - 12.4 Executed Trade Parameters;

- 12.5 Intended Trade Parameters (i.e. those Trade Parameters expected or intended by the National Grid NTS representative when executing the trade);
- 12.6 Details of any actions taken in accordance with paragraph 2 or 3;
- 12.7 Value of the error determined in accordance with paragraph 5 or 6; and
- 12.8 Details of any adjustments made in accordance with paragraph 8 or 9.

### Definitions

13. 'executed' means (in the context of Trade Parameters or cost/revenue) the values (confirmed by the Trading System Operator) at which the trade was conducted
14. 'intended' means (in the context of Trade Parameters or cost/revenue) the values at which the National Grid NTS representative intended to strike a trade;
15. 'Trade Parameters' means the trade price, trade volume and the delivery date (or range of delivery dates) for the relevant gas trade.

## 6 Impacts & Other Considerations

### Does this modification impact a Significant Code Review (SCR) or other significant industry change projects, if so, how?

None identified.

### Consumer Impacts

Consumer Impact Assessment	
Criteria	Extent of Impact
Which Consumer groups are affected?	None - the Workgroup agrees with the proposer's view, as the small potential benefit to shippers of approximately £30k to £90k per annum (0.15% to 0.45% of Operating Margins annual costs), suggests this modification is only going to lead to a negligible benefit to consumers.
What costs or benefits will pass through to them?	n/a
When will these costs/benefits impact upon consumers?	n/a

Are there any other Consumer Impacts?	None identified.
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## Cross Code Impacts

None.

## EU Code Impacts

None.

## Central Systems Impacts

The systems required for the tender process and sale of gas are already in place via the exchange or OTC. Therefore, there are no systems changes required only minor amendments to the process for reprofiling and SMPS by National Grid NTS.

## Workgroup Impact Assessment

The Workgroup sought clarification of several matters closely associated with this change. These can be summarised below:

### *Self-governance status*

The Workgroup agreed with the Modification Panel's determination on Self-Governance as the modifications potential reduction in costs for Shippers (up to £90k per annum) and update to the process (to be more reflective of the current market) is unlikely to have a material impact on competition.

### *Operating Margins related trading*

The Workgroup asked what trading platforms can be used and what licence restrictions/ limitations might apply to this activity. National Grid NTS clarified that the trading platforms available are brokered markets, Over the Counter (OTC) and trading exchanges such as ICE Endex.

The Workgroup also asked what the publishing requirements were with regards to NTS trades (current/proposed). National Grid NTS clarified that no changes were proposed. Currently Operating Margins Gas tenders and results are published and Operating Margins gas data trading is published in the annual Procurement Guidelines Report.

### *Operating Margins related incentives*

The Workgroup asked for details of any related incentives and clarity on which party (ies) bears the costs in the event of a trading error made by National Grid NTS. National Grid NTS clarified that there are no incentives for Operating Margins gas and any Trading errors would be borne by Shippers but it is a low probability that a mistake could occur for a trade (or a tender for that matter). The work group requested National Grid NTS to clarify if any shrinkage manifest trading errors have been apparent.

The following information was provided:

- 5 shrinkage trading errors have occurred in the past ~10 years
- In each case, National Grid NTS was able to rectify the errors either at cost or with a marginal (~£50) gain / loss due to market movement
- ~500 shrinkage trades are typically conducted per year
- Frequency and materiality of shrinkage trading errors has therefore historically been low
- Such errors have been unwound with minimal cost or at no cost at all

The Workgroup agreed that based on this information the probability of OM trading error was acceptably

low).

## 7 Relevant Objectives

Impact of the modification on the relevant objectives:

Relevant Objective	Identified impact
a) Efficient and economic operation of the pipe-line system.	None
b) Coordinated, efficient and economic operation of (i) the combined pipe-line system, and/ or (ii) the pipe-line system of one or more other relevant gas transporters.	None
c) Efficient discharge of the licensee's obligations.	Positive
d) Securing of effective competition: (i) between relevant shippers; (ii) between relevant suppliers; and/or (iii) between DN operators (who have entered into transportation arrangements with other relevant gas transporters) and relevant shippers.	None
e) Provision of reasonable economic incentives for relevant suppliers to secure that the domestic customer supply security standards... are satisfied as respects the availability of gas to their domestic customers.	None
f) Promotion of efficiency in the implementation and administration of the Code.	None
g) Compliance with the Regulation and any relevant legally binding decisions of the European Commission and/or the Agency for the Co-operation of Energy Regulators.	None

This modification would further relevant objective (c) Efficient discharge of the licensee's obligations, because it will enable National Grid NTS to deliver an efficient and economical solution for reprofiling Operating Margins Gas in storage as per its licence condition.

## 8 Implementation

As self-governance procedures are proposed, implementation could be sixteen business days after a Modification Panel decision to implement, subject to no Appeal being raised.

## 9 Legal Text

Legal Text has been provided by National Grid NTS and is included below.

The Workgroup has considered the Legal Text and is satisfied that it meets the intent of the Solution.

### Text Commentary

Paragraph	Explanation
Deleted paragraph 3.3.7	Deleting this paragraph means that National Grid NTS is no longer required to purchase Operating Margins Gas through a tender. National Grid NTS may choose to run a tender, with the additional flexibility to purchase gas on a trading exchange, over-the-counter (OTC) or brokered markets.
Existing paragraph 3.3.8 renumbered as 3.3.7	The reference to existing 3.3.7 is removed as the requirement to tender under existing 3.3.7 will no longer exist.
Paragraph 3.7.2	The existing language requires NG to conduct a tender before it disposes of Operating Margins gas. The amended wording requires that, consistent with its Licence obligations, NG disposes of Operating Margins Gas in the way in which it considers most economic. As is the case with purchase, National Grid NTS will then have the flexibility to sell on an exchange, or over-the-counter. The amended language also allows National Grid NTS to procure or dispose of Operating Margins Gas before the end of the Storage Year, to reflect the normal practise of making the disposals before the capacity rights reduce or expire.
Amend the remainder of existing paragraph 3.7.2 as 3.7.3	<p>The new 3.7.3 explains that, where National Grid NTS considers a tender is most economic, the provisions that follow will apply to that tender.</p> <p>Paragraphs 3.7.2 (a) to (f) have been renumbered as 3.7.3 (a) to (f).</p> <p>New 3.7.3 (g) provides that National Grid NTS need not accept the highest or any tender and mirrors paragraph 3.3.6(c), which applies to buy tenders. It replaces existing (g) which required that National Grid NTS accepts the highest priced tender(s) first.</p> <p>New 3.7.3 (h) provides that any gas unsold following a tender may be sold by other means. It replaces existing (h) which dealt with how tenders would be accepted but was unnecessarily prescriptive.</p>
Existing paragraph 3.7.3 renumbered as 3.7.4	No text change.
Existing paragraph	Existing 3.7.4 is deleted and is, in part, dealt with in new 3.7.3 (h) – see

3.7.4 and new 3.7.5	above. The cost recovery element of existing 3.7.4 is dealt with in a new 3.7.5.
Existing paragraph 3.7.5 renumbered as 3.7.6	This is amended to reflect that fact that Residual Gas Transfers may be made otherwise than by tender.
Existing paragraph 3.7.6 renumbered as 3.7.7	No text change.

## Legal Text

### UNC TPD Section K

*Delete existing paragraph 3.3.7:*

~~3.3.7 National Grid NTS will make its Margins Gas Procurement Arrangements for material quantities of gas under paragraph 3.3.5 on the basis in paragraph 3.3.6(c) where reasonably feasible in the circumstances (and having regard to the time or times for delivery of such gas); and in any case where such arrangements are not made on such basis agrees to inform Users of the circumstances in which its arrangements were not so made.~~

*Renumber existing paragraph 3.3.8 as 3.3.7, and amend to read as follows:*

~~3.3.8~~ 3.3.7 Without prejudice to paragraph ~~3.3.7~~, National Grid NTS may procure gas (in accordance with paragraph 3.6) for Operating Margins Purposes and on behalf of the NTS Shrinkage Provider on an integrated basis; but National Grid NTS shall in any event maintain separate records of the quantities of gas procured for Operating Margins Purposes and the NTS Shrinkage Provider.

*Amend the lead in to existing paragraph 3.7.2 to read as follows:*

3.7.2 National Grid NTS on behalf of each Relevant System Manager will before, or as soon as reasonably practicable after, the start of each Storage Year make such arrangements for, ~~as soon as reasonably practicable after the start of the Storage Year, seek to make~~ Residual Gas Transfers as it shall determine to be the most economic for the discharge of its functions under this Section K, ~~in respect of the Residual Surplus Gas in each relevant Storage Facility or LNG Importation Facility by conducting a tender as follows:-~~

*Amend the remainder of existing paragraph 3.7.2 as follows by making it paragraph 3.7.3 and by adding the following highlighted text to the lead in; and by deleting existing paragraphs (g) and (h) and replacing them with new paragraphs (g) and (h) (as highlighted):*

3.7.3 Where National Grid NTS, with a view to meeting the objectives in paragraph 3.7.2, conducts a tender:

~~(g) National Grid NTS will accept bids in order of price (the highest priced being accepted first) for the whole of the quantity specified in each bid (subject to paragraph (h)) until it has accepted bids for that amount of gas equal to the difference between the aggregate remaining surpluses and the aggregate remaining deficits as determined by National Grid NTS in accordance with 3.6.4 (provided that National Grid NTS shall not be required to accept bids for Residual Surplus Gas at a relevant Storage Facility or~~

~~LNG Importation Facility in excess of the amount of Residual Surplus Gas at such relevant Storage Facility or LNG Importation Facility);~~

~~(h) the last bid (for the lowest price) accepted may be accepted for a part of the quantity specified in the bid, and if more than one such bid has the same price such bids will be accepted pro rata the amounts of each, disregarding any bid which states that it may only be accepted for the whole of the specified quantity.~~

(g) National Grid NTS shall not be required to accept the highest priced or any bid where in its reasonable opinion a prudent seller of gas in comparable circumstances would not do so; and

(h) if after the tender the Residual Surplus Gas, or any part of it, is unsold, National Grid NTS (on behalf of Relevant System Managers) will take such other reasonable action as it shall think fit to dispose thereof.

*Renumber existing paragraph 3.7.3 as 3.7.4 and there are no changes to the text.*

*Delete existing paragraph 3.7.4:*

~~3.7.4 If after the tender under paragraph 3.7.2 there is any remaining Residual Surplus Gas, National Grid NTS (on behalf of Relevant System Managers) will take such other reasonable action as it shall think fit to dispose thereof (it being apparent that no User is willing at any price to enter into a Storage Gas Transfer thereof); and any reasonable costs incurred by National Grid NTS in so doing (including costs incurred by reason of having gas in storage in excess of its Storage Space or LNG Importation Space) shall be costs of the Relevant System Manager for the purposes of this Section K.~~

*Insert new paragraph 3.7.5 to read as follows:*

3.7.5 Reasonable costs incurred by National Grid NTS in making Residual Gas Transfers (including costs incurred by reason of having gas in storage in excess of its Storage Space or LNG Importation Space) shall be costs of the Relevant System Manager for the purposes of this Section K.

*Renumber existing paragraph 3.7.5 as 3.7.6, and amend to read as follows:*

~~3.7.5~~ 3.7.6 Where more than one Relevant System Manager holds Residual Surplus Gas in a Storage Facility or LNG Importation Facility, the gas-in-storage subject to Residual Gas Transfers and the proceeds of the ~~tender under paragraph 3.7.2 and any costs under paragraph 3.7.4~~ Residual Gas Transfers will be apportioned pro rata their respective quantities of Residual Surplus Gas in the facility.

*Renumber existing paragraph 3.7.6 as 3.7.7 and there are no changes to the text.*

## 10 Recommendations

### Workgroup's Recommendation to Panel

The Workgroup asks Panel to agree that:

- Agree that self-governance procedures should apply
- Be issued to consultation.