UNC Workgroup 0435 Minutes
Arrangements to better secure firm gas supplies for GB customers

Monday 17 December 2012

ENA, 52 Horseferry Road, London SW1P 2AF

Attendees

Tim Davis (Chair)	(TD)	Joint Office
Lorna Dupont (Secretary)	(LD)	Joint Office
Alan Raper	(AR)	National Grid Distribution
Antonio Ciavolella	(AC)	BP Gas Marketing
Charles Ruffell	(CR)	RWE Npower
Chris Wright	(CW)	Centrica
Claire Thorneywork	(CT)	National Grid NTS
Darren Lond	(DL)	National Grid NTS
Elsa Wye	(EW)	Statoil UK
Erika Melen	(EM)	Scotia Gas Networks
Julie Cox	(JCx)	Energy UK
Lorna Lewin	(LL)	DONG Energy
Mark Cockayne	(MC)	Xoserve
Mark Dalton	(MD)	BG Group
Tom Farmer	(TF)	Ofgem

1. Introduction

TD welcomed all to the meeting.

1.1 Review of Minutes

The minutes of the previous meeting were accepted.

1.2 Review of Actions

0435 11/03: All to consider whether it would be beneficial for National Grid NTS to be able to contract directly with customers.

Update: Under consideration. **Carried forward**

0435 11/04: Ofgem (TF) to provide clarity around Ofgem's SCR position with regard to essential requirements for DSR and consumer compensation.

Update: TF set out Ofgem's position, see 2.0 below. **Closed**

0435 12/01: *Operating Margins (OM)* – Clarify what communications are made, via what route and to whom.

Update: DL confirmed that primary communications were sent to the party holding the contract (generally this is the Shipper) and to a second contact on site if the primary contact was unavailable. It was prudent to have a number of available contacts. **Closed**

2. Update from Ofgem SCR Meeting (14 December 2012)

TF gave a presentation outlining what had been discussed at Ofgem's High Level Roundtable meeting. Some areas of common ground had been identified, and Ofgem was exploring some areas in greater depth. Some key considerations for alternatives were outlined, together with high-level next steps. A general discussion ensued.

Areas of Common Ground

EW asked for a clarification of the term "recognition" – who did this involve? Was it a consensus, or some parties?

CW asked for a clarification of the term "keeping the market open". TF indicated that this was a Shipper to Shipper trade approach, and included setting cashout. MD commented that £20 per therm destroys markets. AC believed the cashout price ought to be kept open as late or as long as possible. TF indicated that it was a general feeling that anything that can be done to avoid freezing it out too early would be welcomed.

JCx reported that the meeting's discussions had centred on general principles and issues in an effort to identify any commonality of views between industry and Ofgem, and a greater level of detail had yet to be approached. Views were not too far apart. TF added that presentations from the meeting would be published on Ofgem's website.

CT suggested that, for definition purposes, anything not allocated through the NDM process should be considered as able to participate in the DSR process.

Key considerations for alternatives

EW expressed concern that cashout prices could end up unreasonably high if based on a single extreme transaction, for example if National Grid saw no alternative but to accept very high priced offers. CT commented that prices could be set by different circumstances; in an emergency National Grid NTS was not in the market and its actions would not feed into market prices (only through PEC) since control and command would be invoked.

Next Steps

TF will report back on the areas that Ofgem indicated were subject to further consideration. CW asked if it was still Ofgem's intention that it would use its SCR powers to implement 'extras' on top of any UNC modification. It would be important to avoid a disjointed and fragmentary approach. The UNC route was transparent and also provided the opportunity to raise alternatives.

EW welcomed the positive approach from Ofgem that had opened up this area to further industry debate.

EW asked if the Security of Supply Report was to be revised; TF was unable to confirm this at present.

Asked if Ofgem anticipated a series of meetings to take the issues forward, TF indicated that he was not aware of any plans at present, but will feedback that the opportunity for further involvement and participation was very much welcomed and valued by the industry. TD commented that the statement "We will consider with industry how to bring package together" sounded as if a consultative process was envisaged.

3. Revised Modification

CW had produced some draft Business Rules and these were reviewed and discussed.

Establishing and securing the required volume

CW explained that the modification intends to create a much smoother curve and provide more appropriate price signals regarding the cost of supply loss. CW would welcome views on whether the proposals under 0435 should stop once a GDE is declared, or go beyond. The modification was focused on avoiding getting into an emergency; the modification could therefore be stopped at the point of emergency, or it could encapsulate arrangements that take place once the emergency has been declared.

The intention was for payment to be to customers, not Shippers. TD asked who would make the payment – the UNC is a contract between Shippers and Transporters. Compensation to third parties could not be mandated through the UNC - any matter between the Supplier and the customer is not a UNC issue.

EW observed that there may be a real risk of mismatch between 0435 and a GDE, and customers would need to be incentivised to bid into a DSR auction. CW explained how the 0435 incentive might work. This gave rise to a number of questions: Should parties who do not take part in the auction also receive a level of compensation? Does it include DM customers that are involuntarily curtailed?

MD believed that a party that did not participate should not be better off than those who had participated in the auction. To get meaningful DSR auctions, the arrangements need to move away from £20 per therm. CW indicated that 0435 has taken a view on compensation, ie an exercise fee for participants, and nothing if not participating. AR suggested an alternative might be that, rather than nothing, non-participants receive the lowest offered exercise price. CW thought this might weaken the argument to take part in the process.

Bullet Point 1 – CW explained how the scope had been widened and to whom it was now available.

Bullet Point 2 – CW has discussed setting a security standard with DECC and this is under consideration; further clarity is needed. If DECC do not set an alternative, then it will default to the EU standard.

Bullet Point 3 – CW explained how he saw this working; inefficient outcomes in the first round would result in a second round to enable better price discovery. DL suggested that a methodology might be required to establish/clarify what an inefficient price would be (validated by the industry and not left to National Grid NTS' discretion). A mechanism to establish an efficient price was required; accepted/rejected prices, tolerances etc were briefly discussed, and whether parties would feel encouraged by an unsatisfactory outcome to then participate in a second round.

To manage the maximum exposure and encourage participation, as well as avoiding the need to establish a target volume in advance, AC suggested National Grid could be given a maximum budget to spend on securing contracts. As a backstop to avoid accepting unduly high bids, TD suggested the cost of investing in a linepack store (not available as commercial storage) could be adopted; if this was cheaper than the bids received, this could be an alternative solution that would remain available in future.

EM questioned if customers had to choose between different types of interruption. CW indicated that they would have to demonstrate the ability to meet the contracted services; perhaps there should be a hierarchy of priority. Clear rules might be required. The potential for a customer to be paid twice was considered.

MD asked if there should be different services for NTS (commodity) and DN (transportation) support. This would be solving the same problem (shedding load) – but would require option fees for 2 different things. It was not seen as a problem to exercise both, or even both on the same day. CT gave examples of where this might apply. Keeping parties off/turning back on within and next day may be the issue. CW explained how the option/exercise fees might work. TD reiterated that it should be kept simple for what was expected to be an exceptionally rare event. EM indicated the DNs were concerned if interruption tenders would be affected since parties believe they are sufficiently covered.

TD asked if National Grid NTS should establish a target volume and referred back to AC's suggestion of setting an allowed revenue. TF briefly touched on an alternative approach based on an exercise only price/stack that National Grid NTS would work through (i.e. no option fee), which could be procured without defining a volume. CW reiterated that customers desired the ability to turn down in tranches. TF indicated this would require consideration, as opposed to necessarily requiring an option fee.

TD pointed out that one view was that customers need to be funded to invest in some sort of back up to keep plant on, and some incentive was required so that the industry can call upon the DSR mechanism to assist in an emergency situation. Customers need to see some sort of benefit. On the other hand there might be an argument to say that customers would be investing now in back up anyway (prudent business). Would the reality be any different?

CW asked what would be considered to be the efficient price to pay for this service. Would eventual option fees actually cover this? Should it be a zero option or very low, or just bid an exercise fee? Views were sought.

JCx believed something was required to bring parties on board. If a party was going to be called off anyway they would get something from the exercise fee. MD reiterated it was important that a party should not benefit if not actively participating. Communications and contracts between parties were briefly discussed. Reference was made to bi-laterals (which had not worked) and there was some doubt that this would actually improve the situation. An option fee might be more encouraging because of the unlikelihood of the event. CR indicated a liking for the suggestion of option fees/stacks, and pointed out that the industry should not be funding what could be seen as an income stream for manufacturers. TD pointed out that the costs of compiling a bid, or the building of back up facilities, would vary depending on the customer concerned.

JCx suggested a capacity discount for participation. DL suggested fixed option fees for different location bands. CW observed that in his experience customers would want the flexibility to choose their exercise and option payment. EW thought these would need to be cost reflective. Both JCx and EW pointed out that customers really required more awareness of the issue, and EW reported that customers would prefer to contract with National Grid NTS direct rather than with the Shipper, seeing this as being more transparent; there was always an element of concern from the perspective of the customer as to the reason why they were being asked by a Shipper to interrupt. MD questioned, if this were to be the case, how payments would be made.

Referring back to bullet point 2, CW indicated alternatives could be allowed revenue for National Grid NTS, or run the process and then pass all the information to Ofgem and leave it to the Authority to establish the Security standard and an efficient price; Ofgem may prefer to refer it to DECC. TD commented that National Grid NTS would expect to be funded, and Ofgem would inevitably be asked to address allowed revenue issues.

CW asked, what would be the most credible scenario and realistic shortfall in the time horizon; how could the right price for the volume required be struck? TD observed it was hard to set the volume and assess a reasonable price – should there be a backstop? When should offers stop being accepted? There were no easy answers to volume and price setting. DL asked what would happen if not enough was tendered.

CW asked if the best way of doing it at the moment is to establish a security standard. JCx suggested it would be simpler to set a volume of Xmcm, with DECC and National Grid NTS to establish the volume. MD added that it also depended on the scale of available interruptible load.

TD suggested that it might help if a first draft of a methodology for accepting offers were to be written. DL agreed to consider what might be required for this. Other views would also be welcomed.

Action 0435 12/02: *Business Rules -* Consider what might be required for the development of an appropriate methodology for accepting offers.

MD felt SSR should be excluded, and observed that a supply side party would consider flexibility might be better offered on the day rather than tying this up in advance. CW responded that parties have expressed a willingness to do certain things in return for an option fee every year.

OM Gas

OM gas is system support; this gas is balancing gas and feeds into cashout. DL commented that comparability and the ability to merge the products might depend on the timescales and what the security standard is.

MD observed that the SSR side is largely catered for by parties being responsive at the time. TF indicated that this approach had been seen as a way of the demand side accessing the market and revealing their VoLL. Referring to SSR and avoiding a GDE, CW gave Rough as an example whereby cushion gas might be called upon; this would be expensive, but better than getting into a GDE. JCx thought the ability/timing to call on cushion gas might be a problem on high demand days when Rough might already be exporting at its maximum capability. However, it would seem better to try and call in everything to try and avoid a GDE in the first place. Would there be any issues with National Grid NTS contracting with storage facilities with multiple Shippers, eg Rough?

CW asked if it was thought that SSR should be part of this modification? MD thought not; he saw this as harmful rather than neutral and intended to contact CW explaining his view. He believed it should be kept simply focused on DSR and cashout treatment. TD confirmed that the consensus view was that OM gas should not be included.

Treatment of costs and cash out prices

CW explained option fees. MC confirmed that he could not see any systems problem in utilising the 15th day of the month as a reference point for a snapshot.

MD remained of the view that the market was potentially distorted by applying costs to Entry; AC agreed. TD observed that reflecting National Grid NTS' costs was the test for transportation charges, although it was unclear what the cost driver is and hence how charges should be applied. JCx believed this to be an SO cost, and SO costs are recovered 50:50 between entry and exit – it is not clear why this cost should be treated differently. Acknowledging MD's comment, TD said that he understood MD's view from a benefit, as opposed to cost, reflective perspective. DL confirmed that OM is an SO cost and hence is recovered equally from entry and exit charges. CW indicated that he would welcome any compelling arguments for the charging arrangements that should apply, but recognised that an arbitrary judgement might have to be make.

Exercise fees were then discussed. JCx believed the proposed approach to be similar to ECQ except that the customer receives a payment for not delivering the gas. The detail of what happens if a party is already turned off (eg for maintenance) and what should then be done to make sure they do not turn on again until instructed needed consideration. Should they be paid *not to come on*? Should the Shipper not be paid the 30 day average SAP because it was not delivering the gas? Tranches and associated issues were briefly discussed. It needed more thought to achieve the best outcome in the simplest way possible.

CW asked if the proposed approach worked for SSR, and various scenarios were discussed. Disparate views were expressed as to whether an exercise fee should be applied. How to maintain stability of delivery or the opposite was discussed. TD observed that parties would already be expected to be operating to provide maximum gas in an emergency, and calling on 'extras', such as cushion gas or something that has been specifically contracted to National Grid NTS - eg an extended linepack store - to extend capability for just such an eventuality.

The two elements associated with the cost of exercising any option both made sense to JCx, but she added that non-delivery of service should be explored because it would already be maxed out. Ofgem was keen for options to be explored, including SSR, and taken into account/discounted if necessary, with the inclusion/exclusion being justified.

CW reiterated that the focus was on *not* getting into a GDE. MD believed that flexibility would not be committed in this way; it can be done through OM now; it cannot be used twice – either for system support, or the even more rare event of GDE. OM does not lead to 5mcm being contractually held back, where as it is being held back under the proposed approach. MD would strongly prefer the SSR bit to be excluded (it complicates the issues and is a less optimal solution). JCx questioned if cushion gas was separate/unique and needed thought. TD believed that it came back to specific examples of gas not otherwise available to the market.

If SSR stays in then consideration needs to be given to: why? What would be appropriate charges and how delivered? Contractual delivery? Failure to deliver service? Links to cashout? Status of sites already off (eg for maintenance) and how exercise fees should be applied, and how to ensure not to come back on? Against what volumes would a party be paid? Or tranches? For how long – one fee for the complete day?

MD thought that some certainty of performance should be ensured/demonstrated. AR thought that there was no way of knowing exactly what each individual site would otherwise have done. MD suggested that some measure of performance would still be required, ie to show that they have responded and reduced demand. TD suggested a requirement to flow no more than Y, rather than reduce by X.

JCx referred to ECQ; tranche arrangements add complexity but this is what customers have said they would consider. It needs to be kept simple. CT commented the product would be used as part of a package of tools, depending on how much time is available. The market would be expected to be already responding. By the time the expensive exercises are reached, the chances are that National Grid NTS would be already taking balancing actions. CW thought this brought it back to establishing an efficient price and paying up to that. JCx asked what volumes is this paid against?

CW noted the points made in discussion and intended, with National Grid NTS, to give more thought to the balance between efficient cost allocation and getting something that works for most parties.

Contributions to exercise fees were considered. All parties who physically flowed would be ‘hit’ (demand and supply). There may be a hefty neutrality charge but this can prevent escalation of the issue. MD suggested doing some calculations to verify potential costs. The neutrality element will have to be factored/priced in, in advance; caps to be in place?

Responding to a question from JCx (Business Rules page 3, bullet point 2), CW indicated that cashout would freeze at this point, contingent on where the ‘efficient’ line was drawn, so it has to be clear where the price/volume target was set. There was a brief discussion on how the NEC would call loads off in an ‘immediate’ or ’fast’ emergency for safety reasons, and how this might affect commercial cashout (assumes DSR is irrelevant in this scenario). TD commented that in a ‘fast’ situation the NEC would have called everyone off over a compressed timescale. There was an argument to suggest that if the exercise price was too high to reasonably call, then it should not have been accepted in the first place.

CW indicated that if there was no DSR price escalation, we could potentially enter a GDE with a very low cashout price, and Ofgem has already indicated concerns if it is too low. There may be a number of solutions to consider and CW gave some examples, which took account of likelihood and perhaps might provide more certainty to parties regarding costs. JCx suggested developing scenarios with ranges of volumes; this was noted by DL.

CW would welcome any further ideas and suggestions and also Ofgem’s view on the options which may or may not be worth taking forward.

The Table summarising voluntary DSR and SSR arrangements was then reviewed. CW reiterated that he was trying to create an incentive to take part and bid at a competitive level. Should there be a principle of compensation for taking part in the process? EM thought this might be open to abuse and would be difficult to control. TD asked, what would be a reasonable bid, and what would be ‘gaming’? A short discussion took place.

Contractual arrangements and communications

This area was considered. TD reiterated EW’s earlier point regarding customer’s preference for direct contracting. However, arrangements for cash out and billing etc made it simpler under the UNC. JCx thought it might fit better outside of UNC so that Shippers had nothing to do with it at all. EM commented that the DNs would need to consider how they linked into customer contracting and communications. CW indicated that he would expand bullet point 1 on page 5 of the Business Rules to include DNs. TD reiterated that the focus should be on managing the situation rather than the Code requirements; a common sense approach. The route to implementing this was secondary.

MD asked how quickly does the exercise price get reflected in the SMP Buy price? TD answered, as now. DL believed there is no way of overriding the APX screen but there may be some datafix that APX can do. JCx believed there needed to be some way of letting parties know that prices are escalating, eg ANS.

Operational Arrangements

It was recognised that certain elements were not pertinent to this modification but would be recommendations in respect of pursuing potential changes to the Gas Transporter Licence.

TF believed the linepack incentive had been considered as part of RIIO and would not be suspended.

Next Steps

CW recognised that further redrafting work was required based on the discussions.

A draft methodology and a revised proposal will be brought to the next meeting for review and discussion.

4. Any Other Business

None raised.

5. Diary Planning

Arrangements will be made for the next Workgroup meeting to be held in January 2013, and will be confirmed when details have been finalised.

Workgroup 0435 - Action Table

Action Ref	Meeting Date	Minute Ref	Action	Owner	Status Update
0435 11/03	16/11/12	2.0	Consider whether it would be beneficial for National Grid NTS to be able to contract directly with customers.	All	Carried forward
0435 11/04	16/11/12	5.0	Provide clarity around Ofgem's SCR position with regard to essential requirements for DSR and consumer compensation.	Ofgem (TF)	Closed
0435 12/01	06/12/12	2.	*Operating Margins (OM)* – Clarify what communications are made, via what route and to whom.	National Grid NTS (DL)	Closed
0435 12/02	17/12/12	3.	*Business Rules* - Consider what might be required for the development of an appropriate methodology for accepting offers.	National Grid NTS (DL)	Pending