

**UNC Workgroup 0555R Minutes
Review of the Market Operator (OCM) Provision
Friday 15 January 2016
31 Homer Road, Solihull B91 3LT**

Attendees

| | | |
|-----------------------------|-------|--------------------------|
| Les Jenkins (Chair) | (LJ) | Joint Office |
| Mike Berrisford (Secretary) | (MB) | Joint Office |
| Adam Lane | (AL) | Centrica |
| Anna Shrigley* | (AS) | Eni |
| Charles Ruffell* | (CR) | (RWEST) |
| Darren Lond | (DL) | National Grid NTS |
| Egbert-Jan Schutte-Hiemstra | (EJ) | ICE Endex |
| Graham Jack | (GJ) | Centrica |
| Julie Cox | (JCx) | Energy UK |
| Laura Langbridge | (LL) | National Grid NTS |
| Lucy Manning | (LM) | Gazprom |
| Nigel Sisman | (NS) | Sisman Energy Consulting |
| Raveena Virk | (RV) | National Grid NTS |
| Richard Fairholme | (RF) | E.ON UK |
| Sirko Beidatsch | (SB) | PEGAS |
| Steve Nunnington | (SN) | Xoserve |
| Terry Burke* | (TB) | Statoil |
| Thomas Farmer | (TF) | Ofgem |
| Wouter de Klein | (WK) | ICE Endex |

* *via teleconference*

Copies of all papers are available at: <http://www.gasgovernance.co.uk/0555/150116>

The Workgroup Report is due to be presented at the UNC Modification Panel by 21 April 2016.

1.0 Review of Minutes

The minutes of the previous meeting were approved.

2.0 Workgroup Discussion

Commencing proceedings, LJ explained that the main focus of the meeting was to undertake consideration and ongoing development of the draft Review Group Report.

2.1. Aggregating data – updates (Actions 1101 and 1102)

In providing a brief overview of the '0555R – Review of the Market Operator (OCM) Provision – Workgroup 3' presentation, LL explained that the presentation had recently been updated in order to incorporate information relating to both the outstanding actions, plus additional key items for consideration and updated (high level only) costs assessment.

In looking at the 'Emerging Scenarios' slide, the consensus amongst those present was that options 2 and 3b are viable, and that 1 and 3a should not be assessed further. Thereafter, scenarios 2 and 3b were considered in more depth, as follows.

In considering the 'Scenario 2 – Cost Vs Benefit Analysis' slide, LL believed that the benefits analysis was self-explanatory. It was suggested that an additional benefit could be added to highlight that, for smaller shippers, the costs to access the market are more beneficial under this option since the number of platforms required to accede to are limited.

When it was suggested that the capability of any potential bidder (and associated costs) needs consideration, LL responded by suggesting that the proposed 5 year tender arrangements would help to control these types of costs – for users, National Grid and bidders.

EJ explained that should ICE Endex lose the tender, or alternatively decide to withdraw their service provision, the 'market' would still have access to the necessary historical data as they (ICE Endex) would still be obliged legally to keep information for 7 years.

Moving on to focus on the 'Scenario 3b – Cost Vs Benefit Analysis' slide, DL explained that this has been the main area of focus for National Grid NTS. In seeking to understand the costs associated with locational / physical markets being on separate platforms, LL believed that National Grid NTS could possibly have sight of these via some form of 3rd party aggregation – EJ suggested that costs of circa £50k - £100k for equipment would not be unreasonable. DL noted that having a split market (locational / physical) could incur additional costs, but these are unclear at this time.

In looking at the high level cost (HLC) related information contained in slides 7, 8 and 9, DL explained that HLCs were appropriate for this review; he would expect more detailed information to be provided in support of any subsequent UNC modification. SN pointed out that there are certain 'fixed' cost elements that only change slightly if more service providers are added to the equation.

When asked whether or not the HLCs included all necessary technology (i.e. level of network resilience / need for new networks etc.), SN explained that the costs had not been assessed at that level of detail and have basically been drawn together based on looking at similar projects.

When considering the multiple membership fees assumptions, some parties felt that consideration of the cost of procuring credit was relevant as well. In appreciating that the cost of providing locational and physical markets is already embedded within the ICE Endex membership fees, it was suggested that in essence this is a (standalone) 'proxy' for these markets and that teasing out more detailed information appertaining to these might incur additional costs. When asked, DL confirmed that the assessment incorporates ICE's latest 2016 fees.

It was suggested that the trading gateway (slide 8, last bullet point) cost assessment might be underestimated as currently indicated (£5 - £15k p.a.), along with the gateway aggregation estimation. It was also suggested that it is not simply futures related costs to consider as there are also back office (service) related costs, even though these may well be consumer specific to a larger degree.

SB highlighted that the PEGAS membership fee of circa £7k also includes locational / physical markets. In considering the fact that the £7k figure includes all three elements, LJ enquired whether or not a (membership cost) guide was available for the single element (i.e. minus locational / physical markets) as far as this scenario is concerned. Responding, EJ explained that the simple answer is this information is not available, and providing it could potentially undermine ICE's commercial position, as (some of) the information is commercially sensitive in nature. SB advised that the PEGAS membership fee for a single element would be circa £6.5k and that locational / physical is provided at no additional cost basis.

In considering the 'Benefit: (*3) Reduction in.....investment in innovation' slide (9), TF enquired whether a view on transactional costs and scale change impacts had been sought. Responding, EJ pointed out that the number of transactions does not necessarily include marginal costs. He also suggested that care is needed in assessing transactional fees / costs where venue moves are involved (i.e. cost of spread and distribution liquidity aspects etc.).

Moving on to consider the 'Summary Cost vs Benefit of Scenario 3b' slide, DL confirmed that ongoing costs had been considered and in order to appreciate these, simply take away £800k (Low case) and £1.9m (High case) from the two respective column totals. When asked whether it is possible to split out National Grid NTS and industry costs separately, DL suggested that whilst it is possible, the resulting information might be misleading. However, if parties could provide feedback relating to this matter, it would be welcomed.

When it was suggested that identifying a net cost might prove helpful, TF also advised that whilst he believes the current approach is sensible, there could also be 'hidden' technological innovations related benefits that could be included. TF also enquired whether or not there are any instances where costs outstrip benefits and visa versa.

At this point in proceedings, attention focused on the PEGAS 'Opening OCM for competition' presentation.

When asked whether the cost assessments (on slide 3) include resourcing costs, SB confirmed that they did.

During consideration of the information provided within the presentation, several parties felt that the information does not sit comfortably, especially the low £4.5 one off set up costs for 'C'. In discussing how costs could be allocated, LJ suggested that this would be via neutrality invoicing mechanisms. When it was suggested that one option might be to get the industry to absorb the tendering costs, it was pointed out that there are potential licencing considerations to adopting such an approach. LJ suggested that one way of understanding the tendering proposals is to think about how the AUGGE process works, whereby a cross industry group has been set up (i.e. pre tendering governance).

Discussions then returned to consider the 'Next Steps / workgroup' slide in the National Grid presentation whereupon LJ suggested that the Review Group Report is basically completed, subject to some additional input after today's meeting.

TF pointed out that Ofgem would be looking to assess cost / benefits on an industry wide basis. Some parties believed that costs to the market participants should also be considered, even if these are difficult to actually quantify and may be commercially sensitive, however this was not a universally supported view. LJ suggested that one option would be to highlight this matter within the Review Group Report and should parties have additional information they could provide to Ofgem (offline), this might prove beneficial.

When SB suggested that we should include more background detail behind the benefits within the option 2 assessment in order to make a more informed and balanced comparison between options 2 and 3b, LL pointed out that whilst this is not only difficult, it also makes an (incorrect) assumption that we are looking at ICE and PEGAS as the only potential service providers. When asked whether seeking an industry view on a preferred option would be a suitable way forward, LJ pointed out that this would only be utilised should the Review Group feel a finite recommendation was necessary. TF suggested that it might be possible to utilise a form of 'breakeven' analysis (similar to how Ofgem undertake such considerations).

When it was suggested that the argument is not simply a cost based one, and that the review should consider the benefits to the market as a whole (i.e. the price of flexible gas etc.), EJ suggested that there are both 1st and 2nd tier costs / benefits at play. He also pointed out that in his opinion, the original Ofgem letter was not necessarily specific around what the actual Review Group output should be, and he remains convinced that there maybe benefit in seeking industry views – in other words get an understanding of companies internal perspectives. However, some participants felt that making a Review Group recommendation in the first place would then assist the industry to make a more informed view. Accepting that there was not clear consensus around the best approach, LJ pointed out that at the end of the day, it is down to National Grid NTS to answer Ofgem’s letter.

When asked for a steer, TF suggested that if the Review Group could indicate a preferred option that would be helpful, but not necessarily essential, although he does feel that more information around benefits would assist Ofgem in making any subsequent decisions.

Summarising, LJ explained that it would seem to be acceptable for the report to provide for two viable options and recommend that some form of additional Ofgem impact analysis would be required to examine the relative economics and merits.

2.2. Consideration of the (draft) Review Group Report

During a very brief discussion on the draft report, since the earlier presentation had covered the key points, it was requested that a single page ‘Executive Summary’ is added to aid the reader.

LL explained that the report is laid out in such a way as to show the journey the Review Group has taken, which should be helpful to any reader who has not been part of the detailed discussions.

In pointing out that there are no real ‘deal breakers’ included in the report, LJ asked parties to read it at their leisure with a view to providing feedback should they feel the need to do so.

When asked if there are any industry initiatives on the horizon that could / would impact on industry views around the costs and benefits of 0555R, LJ advised that he was not aware of any at this time – a view supported by others at the meeting.

When asked whether there is the option to ask Panel to request industry views on the cost and benefits, LJ responded by advising that whilst feasible, that is the very purpose of this industry review. Concluding, it was agreed that further work around the costs and benefits is needed and that National Grid NTS would provide an amended (draft) Review Group Report in due course.

2.3. Review Progress Against the Scope of the Request

In light of discussions undertaken on items 2.1 and 2.2 above, it was agreed to defer consideration of this item until the next meeting.

3.0 Any Other Business

None.

4.0 Outstanding Actions

0555 1101: National Grid NTS (DL/LL) to provide a view on how much it would cost them to aggregate outputs from multiple market exchange platforms, calculate and publish cash-out prices in near real time. If possible, to look at a range of scenarios to understand the cost implications of different time delays.

Update: Please refer to item 2.1 above. **Closed**

0555 1102: ICE (EJS) & PEGAS (SB) to provide their view(s) on what it costs to aggregate outputs from multiple exchanges and publish cash-out prices in near real time, ensuring all assumptions are stated and presented to the Workgroup.

Update: Please refer to item 2.1 above. **Closed**

0555 1103: National Grid NTS (DL/LL) to provide an outline draft of a potential report built around the three questions, with costs, benefits and risks identified for each.

Update: Please refer to item 2.2 above. **Carried Forward**

5.0 Next Steps

The next meeting will consider the following areas:

- Further consideration of the National Grid NTS draft (outline) report
- Review progress against the Scope of the Request

Meeting papers and action updates should be provided to the Joint Office by 15 February 2016 in preparation for the next meeting.

6.0 Diary Planning

Further details of planned meetings are available at: www.gasgovernance.co.uk/Diary

Workgroup meetings will take place as follows:

| Time/Date | Venue | Workgroup Programme |
|-------------------------------------|------------------------------------|--|
| 10:00 Friday 26 February 2016 | 31 Homer Road, Solihull B91 3LT | Agenda items to be discussed: <ul style="list-style-type: none"> • Further consideration of the National Grid NTS draft (outline) report • Review progress against the Scope of the Request • Review Group recommendation |
| 10:00 Wednesday 30 March 2016 | 31 Homer Road, Solihull B91 3LT | <i>Detail planned agenda items.</i> <ul style="list-style-type: none"> • <i>To be confirmed</i> |

Action Table

| Action Ref | Meeting Date | Minute Ref | Action | Owner | Status Update |
|--------------|--------------|------------|--|---------------------------|-----------------------------------|
| 0555 1101 | 27/11/15 | 2.1 | To provide a view on how much it would cost them to aggregate outputs from multiple market exchange platforms, calculate and publish cash-out prices in near real time. If possible, to look at a range of scenarios to understand the cost implications of different time delays. | National Grid NTS (DL/LL) | Update provided. Closed |
| 0555 1102 | 27/11/15 | 2.1 | To provide their view(s) on what it costs to aggregate outputs from multiple exchanges and publish cash-out prices in near real time, ensuring all assumptions are stated and presented to the Workgroup. | ICE (EJS) & PEGAS (SB) | Update provided. Closed |
| 0555 1103 | 27/11/15 | 2.3 | To provide an outline draft of a potential report built around the three questions, with costs, benefits and risks identified for each. | National Grid NTs (DL/LL) | Carried Forward |