Transmission Workstream Minutes
Tuesday 09 November 2010
Radisson Edwardian Grafton Hotel
130 Tottenham Court Road, London W1T 5AY

Attendees

Tim Davis (Chair)	(TD)	Joint Office
Bob Fletcher (Secretary)	(LD)	Joint Office
Andrew Pearce	(AP)	BP Gas
Antonio Ciavolella	(AC)	BP Gas
Chris Wright	(CW)	Centrica
Claire Thorneywork	(CT	National Grid NTS
Fiona Strachan	(FS)	Gazprom
Ian McNicol	(IM)	Ofgem
Jacopo Vignola	(JV)	Centrica Storage Ltd
Julie Cox*	(JC)	AEP
Nick Reeves	(NR)	National Grid NTS
Rekha Theaker	(RT)	Waters Wye Associates
Richard Fairholme	(RF)	E.ON UK
Ritchard Hewitt	(RH)	National Grid NTS
Shelley Rouse	(SR)	Statoil
Stefan Leedham	(SL)	EDF Energy
Thomas Molnes	(TM)	ExxonMobil
Tim Wyndham	(TW)	Ofgem

**via teleconference*

1. Introduction

Copies of all papers are at http://www.gasgovernance.co.uk/tx/091110.

TD welcomed attendees to the meeting.

1.1 Review of Outstanding Actions

Action TR1001: Provide evidence regarding the influence of default cash out arrangements on balancing behaviour

Update: There was no evidence provided at the meeting. TD emphasised the importance of Shippers providing evidence if a reliable assessment was to be made of the impact of changing the default values. **Action Carried forward**

Action TR1002: National Grid NTS to reconsider the impact of Proposal 0333 on the Relevant objectives

Update: See item 2.1.1 **Action Completed**

Action TR1003: Identify any analysis particularly required by Ofgem in respect of Proposal 0333

Update: TW advised information was required from National Grid with regard to operational costs. **Action Carried Forward**

2. UNC Modification Proposals

2.1 C27 Balancing Arrangements – associated Modification Proposals

2.1.1. Modification Proposal 0333: "Update of the default System Marginal Buy Price and System Marginal Sell Price"

NR introduced the Proposal, explaining that its origins were from Review Group 0291. He described the Proposal objectives and its development to date, including consideration of alternative solutions.

NR presented graphs showing balancing performance from a Shipper and Transporter view point. RH asked if there were any views, on the imbalance analysis shown. CR questioned whether it would be understood as intended – the analysis did not demonstrate the impact of default values on balancing behaviour, nor suggest there was a problem which needed to be addressed. FS was not convinced the evidence was of any clear trend nor that the factors behind change were demonstrated – for example, were 2005 and 2006 atypical years, in which issues such as the Rough outage may have affected cashout performance.

RH agreed there were a number of factors that feed into imbalance. TD asked whether the downward trend was evident this year, and NR thought experience was similar to the trend shown.

The reduction in energy volume through National Grid balancing actions was noted. FS asked if the reduction was due to National Grid becoming more comfortable operating under the current market rules. RH accepted that greater knowledge and experience informed behaviour. SL was concerned about drawing inappropriate and unproven conclusions from looking at a graph. – for example, the number of balancing actions dipped during the year when Distribution Networks were sold, but that did not prove this was the reason why.

CW agreed that a significant number of factors, such as weather, were likely to affect balancing performance and these had not been considered. NR considered Shipper imbalance to be the biggest impact on the volume of National Grid trades. TW agreed that all factors would need to be examined to fully understand the impact on balancing and residual trades. TW also wanted to understand the implications of reflecting short run and long run costs in default values, the impacts on balancing behaviour, and secondary impacts on market liquidity.

CR questioned the objective – what change in performance is hoped for at the end of this process and how would success be measured. TD asked why the presumption is that optimal cashout and residual balancing volumes should necessarily be lower than at present.

RH suggested that he key question was understanding the impact of default cashout – would regime performance be improved if the defaults were changed. Also, if National Grid undertakes more balancing actions as the monopoly system operator, is this is a sign of inefficiency such that steps should be taken to reduce involvement?

FS was not clear there were any improvements which might be driven by amending default cashout. However, if the defaults were significantly reduced, or even removed, this could have an impact on liquidity. She concluded that a balance needs to be retained.

RH asked, if cashout defaults were increased, what would be the impact on the market - would it drive Shippers closer to balance? SL advised this had been discussed in the electricity market and created different set of issues as it potentially impacted market liquidity.

TD asked how the process was going to be moved forward. Was there any benefit in debating the issue at subsequent meetings or is it to be left for views to be expressed in representations? Should more statistical analysis be undertaken to try and inform the way forward?

RH was keen to hear view on Shipper's behaviour in light if a change in risks - if Cashout was changed to SAP or ten times the current factor, what would the impacts be? While willing to provide supporting analysis that is within National Grid's gift, he did not believe further regression analysis would help to address these issues.

RH accepted that the data does not point to an immediate problem, but argued that this does not mean the industry should not be trying to improve the situation – such as by reducing National Grid's balancing actions to zero. RT did not believe it had been demonstrated that it is more efficient for Shippers to undertake lots of small actions rather than National Grid undertake one large balancing action on everyone's behalf.

RF was concerned about introducing incentives to drive National Grid out of the market, as they would always have a role, even if it were residual. RH asked if there was a view on the number of balancing actions National Grid should take. SL had no issues with the number of actions taken, just their timing in the day – a trend towards actions towards the end of the Gas Day had been noted within EDF, and this was undesirable. Others were not aware of any such trend, but RH agreed to check if there was any evidence to support this.

TW explained Ofgem's concern that charges should be cost reflective, and costs should be allocated to those who cause them. The costs of balancing actions do not always directly affect the Users who directly or indirectly instigate the action, particularly because costs are allocated on the day an action is taken. If the linepack incentive were to be removed – which had been suggested by respondents to previous consultations – the need to allocate costs appropriately between days would need to be addressed. TW suggested it was important to understand the cost of linepack usage – is it better or worse to use linepack to balance the system or incentivise Shippers to take their own balancing actions? RT and RF noted that the potential linepack product and its associated costs impacted this.

TD asked if the key is getting prices right - the appropriate actions will follow? TW suggested that the full impacts on the market would need to be understood before concluding this was the case.

RH asked, if there was a reduction in the default price, would there be more efficient industry imbalance costs, and how would this be delivered? JC thought it was difficult to demonstrate any impact until the change is made, with expected impacts being anecdotal up to that point. SL agreed, and considered any change would be a marginal benefit at best since Shippers already aim to balance.

RH then explained that Proposal 0333 is based on the National Grid's costs, including a TO element. SL questioned why charges should include a capacity element when there is sufficient capacity in the system to manage linepack swings. RH clarified that National Grid does not invest for within-day flexibility, but this Proposal is about between-day flexibility and it is reasonable to allocate the costs of pipeline space to those using it. FS raised that there was also no recognition of additional flexibility sources, both in Distribution Networks and through tools besides linepack. RH felt the issue was about identifying the operational cost faced by NTS and ensuring it is funded correctly. RT wanted to understand why there was any shortfall in TO funding, and why any revenue from a new charge is not returned to the party who initially paid for the associated capacity.

The impact of implementing Proposal 033 on the Relevant Objectives was then considered.

TD questioned whether altering the default factors would impact system operation. RH considered it would, as National Grid's actions impact market liquidity and changing the defaults may impact the number and type of actions. FS did not think there was evidence that there would be a change in balancing actions.

The Shippers present did not consider implementation would impact competition between Shippers.

There was consensus that implementation would facilitate discharge of National Grid's Licence C27 obligation to update the default values.

The Proposal states that implementation would facilitate economic and efficient administration of the UNC, but RH accepted the view put forward by others that introducing an additional annual review process could only be expected to increase the costs of administering the UNC. FS added that changes were being proposed which would soon be overtaken by other industry changes driven by changes to European regulation, such that implementation would be contrary to efficient administration.

Given this assessment of the impact on the Relevant Objectives, SR was concerned how this Proposal was improving the current situation, and hence why change was proposed. AP asked why National Grid does not seek derogation from the licence condition, and TW confirmed that Ofgem would necessarily consider any such request on its merits. TW also advised that Ofgem would welcome views on the way costs associated with balancing should be demonstrated and recovered. RH encouraged all to bring forward their views on the way forward, and added that national grid would work with any other party wishing to raise an alternative Proposal.

TW suggested that any change ought to consider short and long run impacts. However, Ofgem remained to be convinced that it was appropriate to include a TO element in the calculation of operational costs associated with the use of linepack, and hence for these costs to be incorporated in any revised default values. CW was concerned that although in principle the SO element is the real cost and should be included, this would appear to indicate that default values should be considerably lower than at present. Hence the theoretically right answer may be inappropriate in practice when it is acknowledged that the existing process works.

NR asked if there were any alternative options to the Proposal, other than do-nothing and listed the options considered as part of the Review Group 0291 process.

TD asked if, rather than alternative, the polluter pays approach (whereby charges are only applied to those our of balance in the same direction as the system as a whole) could be introduced with any default value and hence is a modification on its own? SL felt it was hard to ignore this issue and its solution. FS asked if it would be possible for National Grid to show the potential balancing impacts within day since Shippers which were being "helpful" by the end of the day may not have been earlier when decisions were taken regarding the need for National Grid balancing actions. RH did not agree with a polluter pays approach as Shippers will react to changing circumstances during the day and it could create a "rocking boat". From a System Operator perspective, the most helpful position for any shipper to be in is one of balance.

TD asked if the market-based uplift option was worth considering. CW did not consider this was a credible option, given the solution needs to be justified on cost reflectivity grounds. RH noted that during discussions in RG0291, the issue was Shippers would not know the impacts within day.

SL asked if the costs of other tools for balancing the system could be reflected in charges. RH suggested using storage is an option but generally is not used by National Grid for redressing Shipper imbalance. Turn down is another option.

NR confirmed that National Grid NTS would amend the Proposal in good time to be issued ahead of the next workstream, when the Workstream Report is due to be completed.

Action TR1102: NR to amend Proposal 0333 based on comments received.

2.1.2. Modification Proposal 0337 – "Introduction of an Inter-Day Linepack Product"

RH explained the current position and ROM costs for this Proposal and what has been assessed in the ROM. Development costs are estimated to be £0.758m to £1.07m and operational costs of £37k to £106k. CT confirmed a new online service is proposed. SR asked how charges would be applied, and RH explained this needed to be developed but the Proposal states it is to be allocated to Shippers. SL did not agree this should be a User Pays services and was still to be convinced. RT asked how costs are to be recovered if Users do not take up the service. RH advised this would be based on the recovery timescale in the Proposal, and then by smearing across all Users should the timeline be exceeded.

SL asked if additional costs would be required for resolving FSA issues. CT confirmed that their legal advised had identified there were no FSA issues as the proposed activities were covered by an existing derogation.

RH then gave a high level overview of the Proposal and its Business Rules. RT asked if the product could be assigned to a third party if you purchased it and did not wish to use it. RH confirmed the product could be offset against other products/trades in the system.

CT then ran through the Business Rules, which TD amended on screen to capture comments made.

New Action TR1103: CT to review the role of the linepack manager and provide an update to the next meeting.

New Action TR1104: CT to amend the business rules based on changes/comments made at the Workstream.

2.1.3. **Hybrid/Cumulative Imbalance options**

Cumulative Deviation (Imbalance) Cashout

NR explained the drivers behind a cumulative approach. RT asked if this is to be a mandatory regime, this was confirmed as so.

RT asked, assuming the linepack incentive is removed, are there likely to be increases in linepack variation. RH confirmed there is a number of potential linepack products available for Users which may impact the level of variation seen. TW advised that linepack volumes will need to be assessed based on influencing factors and this may support amending the linepack incentive. There may be an opportunity to change the regime and for the linepack incentive is removed. RT suggested keeping the linepack incentive as a simple means to encourage appropriate balancing actions by National Grid.

CW was concerned that system balance should be reset to zero at the end of each day. RH confirmed Shipper balance would be maintained by daily cashout at SAP. FS asked why Shippers are set to zero on a daily basis but not on a 5-day position – this appears to be a double hit when parties are commercially cashed out at zero each day and then assessed again after 5 days.

RH went through an example to show how the process could work. This allows more flexibility for Shippers. RT failed to understand how this would benefit Shippers, they would not be able to validate their risk. FS could not see a benefit, so why not retain the linepack incentive that is easier to operate.

TW felt the option allows more flexibility and enables the market to define the value of linepack. RF agreed that there had been a case for looking at the process: however, it has now been looked at and does not appear to show a benefit so he did not support continuing. AP added that the increased complexity and risk was a barrier to new market entrants.

Hybrid Options

RH explained the Hybrid strawman and that it included a number of options which were for discussion only at this stage. He explained the definition of Non MBA day, where no balancing actions take place on either the day or the next day.

RH explained some examples of balancing actions and how prices are to be calculated. CW asked what the impact would be if there were no market balancing actions. RH advised it would be an average of SAP.

FS did not see the logic for being cashed out above market value. RH advised this is not just energy as it includes the use of system flexibility.

RT was concerned that there may be impacts based on the type of portfolio a Shipper has. RH did not agree, as the actions taken by the Shipper will contribute to the balancing actions required by National Grid.

SR asked what happens on day 3 if day 2 clears the imbalance. RH provided a day 3 example. TD asked if each day can be a day 1 and a day 2. RH agreed this was possible.

FS asked if the aim is to incentivise appropriate linepack usage, why are shippers being asked to pay twice – they currently pay for the pipes through use of system charges. RH agreed not all customers will want to use this product, but those that do should pay for the use of linepack flexibility.

The view in the room was these approaches would not benefit the GB market and are moving out of step with the rest of Europe. AC was concerned that these proposals add too much complexity for any perceived benefits that could be accrued.

3. Any Other Business

None raised.

4. Diary Planning

The next Transmission Workstream meetings are scheduled as follows:

10:00, 02 December 2010, at Elexon, 350 Euston Road, London NW1 3AW.

10.00, 14 December 2010, at Elexon, 350 Euston Road, London NW1 3AW (to be a linepack day)

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

Action Log – UNC Transmission Workstream: 09 November 2010

Action Ref	Meeting Date(s)	Minute Ref	Action	Owner	Status Update
TR 1001	07/10/10	2.2	Provide evidence regarding the influence of default cash out arrangements on balancing behaviour	Shippers	Carried Forward
TR 1002	07/10/10	2.2	National Grid NTS to reconsider the impact of Proposal 0333 on the Relevant objectives	National Grid NTS (RH)	Completed
TR 1003	07/10/10	2.2	Identify any analysis particularly required by Ofgem in respect of Proposal 0333	Ofgem (TW)	Carried Forward
TR 1102	09/11/10	2.1.1	Amend Proposal 0333 based on comments received	National Grid (NR)	To be provided in sufficient time to allow publication of a draft Workstream report for discussion at the 02 December meeting
TR 1103	09/11/10	2.1.2	0337 - review the role of the linepack manager and provide an update to the next meeting.	National Grid (CT)	Update due 14 December
TR 1104	09/11/10	2.1.2	0337 - to amend the business rules based on changes/comments made at the Workstream.	National Grid (CT)	Update due 4 December