Minutes of Review Group 0221
Wednesday 07 January 2009
held at
Elexon, 350 Euston Road, London NW1 3AW

Attendees

John Bradley (Chair)	(JB)	Joint Office
Amrik Bal	(AB)	Shell
Andrew Fox	(AF)	National Grid NTS
Bali Dohel	(BD)	Scotia Gas Networks
Charles Ruffell	(CR)	RWE npower
Chris Shanley	(CS)	National Grid NTS
Chris Wright	(CW)	Centrica
Craig Purdie	(CP)	Centrica Storage Ltd
David Linden	(DL)	BP Gas
Gareth Evans	(GE)	WatersWye Associates
Jeff Chandler	(JC)	SSE
John Baldwin	(JB2)	Canatxx Shipping
Paul O'Donovan	(POD)	Ofgem
Richard Fairholme	(RF)	EON UK
Ritchard Hewitt	(RH)	National Grid NTS
Roddy Monroe	(RM)	Centrica Storage Ltd
Shelley Rouse	(SR)	Statoil (UK)
Tim Davis	(TD)	Joint Office

1. Introduction

JB welcomed attendees to the eighth meeting of Review Group 0221.

2. Review of Minutes and Actions from the previous meetings

2.1 Minutes (10 December 2008)

The minutes of the previous meeting were approved.

2.2 Actions from previous sessions

Action RG0221/015: National Grid NTS (CT) to confirm whether the 2% of RAV unsecured credit limit applied to security providers as well as Users.

Update: RH reported that this was still being ascertained. **Action carried forward.**

Action RG0221/017: Refine the straw man taking account of discussions to date.

Update: A revised straw man was presented to the meeting. **Action closed.**

3. Discussion of Straw man/Draft Modification Proposal(s) reflecting previous discussions

National Grid NTS's revised strawman was used to structure discussion. CS indicated that National Grid NTS saw the proposed changes as being complementary to the existing credit arrangements for entry and other transportation charges – not a substitute. It was emphasised that views on this would be welcome.

As part of the implementation arrangements, CS said the intention was that Users would not be able to voluntarily relinquish any existing capacity holdings. However, if sufficient credit cover was not provided, all that User's capacity holdings would be cancelled. JB2 suggested that it may be possible to fail to provide credit, capacity holdings to be cancelled, and then for the same User to repurchase some of that cancelled capacity. This behaviour could be commercially worthwhile - for example, if the User had bought flat capacity but would prefer winter only. CS accepted that practical issues would need to be worked through ahead of implementation, bearing in mind the desire to avoid unintended consequences.

Similarly, National Grid NTS was continuing to look at the practicalities of Users increasing their security levels within a bid window, and would welcome views on how this might be facilitated. CS offered to return to the next meeting with some suggestions in this respect. RM was not clear why providing sufficient credit in advance was inappropriate, with no option to increase cover during the bid window. RH agreed that this would be the purest and simplest way forward.

Action RG0221/018: National Grid NTS to develop possibilities for the three timing options for providing credit: all ahead of the bid window; allowing topping-up within a bid window; providing full credit after closure of the bid window.

DL indicated that his internal advice was that practice with auctions elsewhere in Europe involved a "bid bond", and suggested that National Grid NTS should look at this. RH said he certainly did not want to dismiss this, but that the group had previously wanted to look at protecting the value at risk. DL argued that the risk was the risk of default, not the total value, and suggested that those directly involved in credit management might usefully be invited to attend a subsequent meeting and provide some advice on the way in which similar issues are handled elsewhere.

CW was unclear of the value provided by an industry wide bond as opposed to the industry effectively self-insuring as under the present arrangements. DL thought the key difference was that, by contributing to the bond, Users would be paying additional amounts to provide credit upfront rather than any default effectively being handled through cost allocations after the event.

AB asked whether National Grid NTS faced any revenue risk as a result of default. RH said that revenue was secure, being based on allowed revenue. AB continued that this pointed, for him, towards the benefits of bilateral agreements to provide credit in respect of projects where National Grid NTS was being asked to invest, as is seen on the exit side.

CW questioned how different arrangements, such as the suggested auction bond, would have impacted issues seen to date. It was understood that a bond would have involved all players providing a small amount rather than potentially zero as under the current arrangements, such that defaulting parties would have borne part of any costs.

ACTION RG0221/019: BP (DL) to bring further details about auction bonds to the next meeting.

RF offered to see if he could similarly obtain internal advice on practice elsewhere in Europe.

POD suggested that there were two types of risk. First, where incremental investment is involved and second where there is default on baseline capacity. For baseline, allowed revenue is guaranteed and covered by the community whereas for a new venture, somebody is taking a calculated business risk with some of the costs of default potentially passed to other market players.JB2 did not think it was possible to distinguish between incremental and baseline capacity at existing terminals. In his mind, the issue was between infrastructure provided for a single user (i.e. connection assets which nobody else would ever use) as opposed to infrastructure which is part of the general system and potentially used to support a range of Users and entry points.

CS then ran through some options in the strawman for establishing credit worthiness and the consequent requirement to provide credit.

RF raised a concern that the costs of putting the suggested arrangements into place could be more than the likely level of avoided costs. CS recognised that this was a real fear and would need to be reflected in any final solution to ensure it was proportional. CW suggested looking at a real example to assess the implications, perhaps looking at a potential new entry point as a test case for illustrative purposes. CS offered to bring some information to the next meeting based on real numbers such that attendees could see the implications of setting credit requirements at differing levels.

JB2 argued that the key was providing a serious hurdle for bidders to cross, but not one that was unduly onerous. This would help ensure that parties were exposed to some risk and would not enter the auctions lightly.

AB asked whether National Grid NTS has considered taking out insurance against default, the cost of which might help to inform the debate. Attendees were not aware of such insurance having been sought.

CR suggested that there was greater risk when incremental capacity was triggered, and that those who triggered it might be asked to cover 100% of the associated investment cost. JC supported this, but DL was concerned that this could be a barrier to entry. RH argued that the formula put forward in the strawman was seeking to address some elements of differentiation to take account of the wide range of circumstances which could be considered. However DL, while agreeing that risk may vary, felt a simpler approach was worthy of consideration, retaining a level playing field for everyone by looking at their credit position rather than the project involved.

CW suggested that in his mind any step was likely to be a step in the right direction, and he could support almost any of the possibilities suggested since they would be better than doing nothing – we should be wary of spending too long looking for a perfect solution which may not exist. There was general support for this, JB2 emphasising again that requiring a small amount to be at risk would be likely to be sufficient to incentivise appropriate behaviours.

JB asked whether the figures looking at securing bids for Year 4 looked to be of an appropriate order of magnitude and so could be regarded as a way forward? It was accepted that this could be a useful starting point. RH suggested that an alternative would be to look at all auction bids and then apply appropriate percentages to the formula in the strawman such that total exposure was about, say, 10%, but with specific Shipper percentages dependent on their credit position. JB2 suggested looking at the exit requirements with a view to establishing a similar percentage. RH offered to similarly look at the electricity TAR proposals with a view to learning lessons and looking for consistency.

ACTION RG0221/020: National Grid NTS (RH) to present on proposed TAR credit arrangements at the next meeting.

National Grid NTS agreed to bring some possibilities to the next meeting based on this approach, looking at some real data to inform debate.

ACTION RG0221/021: National Grid NTS (CS) to refine the straw man taking account of discussions to date.

In terms of the credit instruments in the strawman, POD was concerned that some of the exclusions may be unreasonable – for example, excluding parent company guarantees could unnecessarily increase cost for the industry. CS agreed to reflect this in the revised strawman.

4. Allocation of actions for next Session 9 (Friday 23 January 2009)

In addition to the actions identified in the minutes, RH agreed to bring a draft Modification Proposal to the next meeting.

ACTION RG0221/022: National Grid NTS (RH) to produce a draft Modification Proposal for discussion at the next meeting

5. Any Other Business

None raised.

6. Diary Planning for Review Group

The next meeting of the Review Group (Session 9) will be held at 10:00 on Friday 23 January 2009, at Elexon, 4th Floor, 350 Euston Road, London NW1 3AW.

Future sessions have been arranged as follows:

Session 10: 13:00 on Tuesday 10 February 2009, at Ofgem Offices, 9 Millbank, London SW1P 3GE

Session 11: 10:00 on Thursday 26 February 2009, at Elexon, 4th Floor, 350 Euston Road, London NW1 3AW.

Subsequent meetings will be arranged as the progress of the work of the group dictates.

ACTION LOG – Review Group 0221

Action Ref	Meeting Date	Minute Ref	Action	Owner*	Status Update
RG0221 015	27/11/08	4.1	Confirm whether the 2% of RAV unsecured credit limit applied to security providers as well as Users	National Grid NTS (CT)	Carried forward to 23 January meeting
RG0221 017	10/12/08	4	Refine the strawman taking account of discussions to date	National Grid NTS (CS)	**Closed**
RG0221 018	07/01/09	3	Develop possibilities for the three timing options for providing credit: all ahead of the bid window; allowing topping-up within a bid window; providing full credit after closure of the bid window	National Grid NTS (CS)	To be presented 23 January
RG0221 019	07/01/09	3	Provide further details about auction bonds	BP (DL)	To be presented 23 January
RG0221 020	07/01/09	3	Present on proposed TAR credit arrangements	National Grid NTS (RH)	To be presented 23 January
RG0221 021	07/01/09	3	Refine the straw man taking account of discussions to date	National Grid NTS (CS)	To be presented 23 January
RG0221 022	07/01/09	4	Produce a draft Modification Proposal	National Grid NTS (RH)	To be presented 23 January

* Key to action owners

RH – Ritchard Hewitt

CT – Claire Thorneywork

CS – Chris Shanley

DL – David Linden