



Gas Transporters and other
interested parties

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value for all customers*

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Date: 2 July 2010

Dear Colleague

Review of consents for Gas Transporter to Gas Transporter services

Background

As part of the sale of four of the Gas Distribution Networks (GDNs) in 2005, the operators of National Transmission System (NTS) and GDNs entered into a range of contractual agreements to provide services to each other and xoserve. At that time, the Authority gave consent to these contracts in the form of an exemption to the de minimis threshold¹.

The effect of such exemptions is to allow a Gas Transporter (GT) licensee to undertake functions that are not within its permitted purpose, to receive related revenues which are not subject to the price control restrictions and additionally to ensure such revenues do not contribute towards the licensee's de minimis limits.

Extensions to the consents for these services have previously been granted on an approximate annual basis. In many cases, as contracts for the provision of these services have expired or the GDNs have either taken over the responsibility for providing these services themselves or contracted with another party to provide them, the need for consent has fallen away. However, during the last gas distribution price control review (GDPCR) it was clear that a number of these contractual agreements still remained, including:

- maintenance services at offtake points;
- emergency assistance services;
- administrative services for Xoserve;
- the provision of the national emergency phone number; and
- a number of transmission services.

In 2008 we decided we should step back and review the remaining relevant consents and how they should be treated beyond their expiry dates, rather than extending these on a case by case basis as and when we receive applications. We issued a letter on 19 December 2008² to consult with industry participants on how best to deal with those services which have been covered by these consents.

¹ Under de minimis arrangements the licence permits the GDN to carry on a business or activity outwith its permitted purpose without seeking Ofgem's consent, provided that the annual aggregate turnover and aggregate amount of such activity does not exceed 2.5 per cent of the GDN's issued share capital or reserves at any time or 2.5 percent of overall yearly annual turnover. De minimis activity is outside the price control.

² This letter can be found at:

[http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?file=Review%20of%20consents%20for%20Gas%20Transporter%20to%20Gas%20Transporter%20\(GT-2-GT\)%20services.pdf&refer=Networks/Policy](http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?file=Review%20of%20consents%20for%20Gas%20Transporter%20to%20Gas%20Transporter%20(GT-2-GT)%20services.pdf&refer=Networks/Policy)

In that consultation letter, we also highlighted that as a result of gas distribution network sales, NGGD provided area control centre services to other GDNs. These services also required consents to be granted to both NGGD and GDNs but at the time of the consultation, it was anticipated that when the relevant consents expired, the GDNs would be operating their own control centres wholly and fully independently of NGGD. We therefore did not consider there was any need to include these services and their associated consents in the consultation.

However, in October 2009, NGGD confirmed that although all the GDNs had indeed established their own control centres, they remain reliant on NGGD's systems to operate their networks. NGGD stated that they will continue to provide some of the services contained within the System Operations Managed Services Agreement ("SOMSA") arrangements to GDNs. NGGD requested that an extension to their SSC A36 consent relating to SOMSA be granted at least until the end of the 2008-2013 gas distribution price control period. Ofgem has considered this request in conjunction with the other consents.

The purpose of this letter is to advise interested parties of a summary of the responses, our considerations and decisions.

The review: aims and options

We set out to consider the following issues:

- which services the GDNs should continue to provide to each other;
- the optimum solution that ensures compliance with the licence i.e. should Ofgem continue to issue consents on a case by case basis or should GTs be permitted to provide certain services on an ongoing basis;
- whether there are concerns relating to the distortion or restriction of competition arising from the continued provision of these services between GTs.

In the 19 December 2008 consultation letter, we also set out the following options for dealing with the costs of the provision of these services:

- Services could be added to the list of permitted activities/excluded services under the relevant licence condition (this is equivalent to granting evergreen consents). This option would be preferred where there is no practical prospect of another party providing these services at an efficient cost. These arrangements would mean that the costs and revenues from these services could become subject to the price control arrangements.
- GTs could be given time-limited consents – for example until the end of the current price control - to exclude the revenue received from the provision of the services from their de minimis limit (this is equivalent to maintaining the status quo). This option would be preferred where there is a practical prospect of another party providing these services at an efficient cost within the timeframe of the consent. This option would also allow us to make the consents conditional on particular actions by the GT. For example if we considered that it was in the interests of customers that the provision of certain services should be unbundled in order to allow third parties to compete for the provision of certain elements of those services, we could impose this condition through the consent.
- Consents could be withheld. In this case, should a licensee continue to carry out the service, costs should contribute towards their de minimis limit.

Ofgem's decision

We have decided to extend all the consents set out in this letter until 31 March 2013 (being the end of the current 2008-2013 gas distribution price control).

We have carefully considered the views of respondents, the impact of extending the consents and whether it is probable that the need for such consents is likely to continue for an extended period.

In our considerations, we recognise the importance of ensuring the continued provision of these essential services and that either withholding consent or proposing a conditional consent may make it unattractive for the relevant service providers to continue providing the services. This would be likely to be detrimental to customers.

We have also carefully considered whether the continued provision of these services by GTs raises any competition issues or concerns. We did not receive any responses expressing concern over the distortion or restriction of competition and it does not appear likely that there are any competition concerns associated with our approach.

We do not believe it is efficient to continue to renew consents on an annual basis. Further, we do not support altering the scope of permitted purpose or excluded services mid-way through a price control period unless there are compelling reasons to do so.

We consider that it is preferable to establish at the next price control review whether it is appropriate to add these services to the list of permitted activities or excluded services, or to keep the consent regime in place.

The appendix to this letter sets out in detail the responses received and Ofgem's decisions for each service.

The published consents can be located at:

<http://www.ofgem.gov.uk/Networks/GasDistr/GasDistrPol/Pages/GasDistrPol.aspx>

If you have any questions regarding this letter, please contact Steve Brown (steve.brown@ofgem.gov.uk / 020 7901 7292).

Yours faithfully



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Appendix: Summary of services, consultation responses and Ofgem views

Services that GDNs provide to National Grid Gas Transportation (NGGT)

Agreement for the Provision of Exit points and General Assets Maintenance Services - consent under Standard Special Condition ("SSC") A36 (Restriction on Activity & Financial Ring fencing)

Under this agreement the GDNs provide services to NGGT at certain NTS exit points located within the GDNs' network including routine and non routine maintenance, emergency services and qualified resources available on a request on a reasonable endeavours basis to support NTS maintenance.

Our initial view was that it would be inefficient for both GDNs and NGGT to maintain the assets. We invited views as to how these services should be provided and on how the costs of the services should be treated.

Responses

The GDNs were the only respondents to this item. They considered it was inefficient for this activity to be undertaken by both parties, that GDNs were better placed geographically than NGGT to offer these services and that there was no impact on competition since alternative third party service providers could be utilised. There was support for it to remain a consented activity on an evergreen basis while one GDN considered it should become an excluded service thereby removing the need for consent.

Ofgem decision

We do not think that there is much likelihood of substantial change in this area within the short term and so we do not consider it efficient to continue to renew consents on an annual basis. However, we do not support altering the scope of excluded services mid-way through a price control period unless there are compelling reasons to do so. We consider it is more appropriate that this issue, and any wider implications, be considered at the next gas distribution price control review. Therefore, we have decided to extend the consents until 31 March 2013 (being the end of the current 2008-2013 gas distribution price control).

Services that GDNs provide to each other

Emergency Assistance Agreement with other GDNs - consent under SSC A36 (Restriction on Activity & Financial Ring fencing)

Under the Emergency Assistance Agreement, the GDNs agree to lend resources to each other and to Independent Gas Transporters to assist in the event of a major interruption of supplies on a distribution network. The agreement deals with the restoration of supplies following a gas emergency and not the emergency response and necessary repairs itself.

Our initial view was that we considered that it is appropriate for the GDNs to continue to provide these services to ensure that customers are reconnected to the gas network in a timely manner. Traditionally this contract has been entered into as a de minimis activity with consent for exemption from the de minimis threshold. However, it should be noted that SSC A41 (Emergency Services to or on Behalf of Another Gas Transporter) places an obligation on the licensee, if directed by the Authority, to enter into an agreement with other GTs for the provision of emergency services including, where necessary, the repair of pipes where a major loss of supply has occurred.

Our initial view was that this licence obligation is not explicitly limited to dealing with the emergency itself but can include resolving the aftermath of an emergency. If the activities currently provided through the Emergency Assistance Agreement were to be included in SSC A41 then this agreement would be treated as an excluded service in accordance with SC E18 (Excluded Services). We sought views on whether it is appropriate to include the Emergency Assistance Agreement within the remit of SSC A41.

Responses

Several respondents felt that there was little likelihood of this crucial service being provided by third parties and that there was merit in the services provided by the Emergency Assistance Agreement being incorporated within SSC A41 or alternatively treating the revenue earned as an excluded service under SC E18. However some concerns were expressed over the impact this would have on the current price control.

Ofgem decision

We do not think there much merit in substantial change in this area within the short term and we do not consider it efficient to continue to renew consents on an annual basis. We do not support altering the scope of excluded services mid-way through a price control period unless there are compelling reasons to do so. We consider it is more appropriate that this issue, and any wider implications, be considered at the next gas distribution price control review. Therefore, we have decided to extend the consents until 31 March 2013 (being the end of the current 2008-2013 gas distribution price control).

Services that National Grid Gas Distribution ("NGGD") provides to other GDNs and xoserve

xoserve – General Services Agreement - consent under SSC A36 (Restriction on Activity & Financial Ring fencing)

Under the General Services Agreement, NGGD provides a number of administrative services to xoserve, including HR services, payroll and communications. The contract will expire in March 2015.

Our initial view was that if NGGD continues to provide these services throughout the price control period we could either amend SC E18 (Excluded Services) to include these costs as excluded services or we could extend the consent until 31 March 2013 and review whether to include these services in SC E18 as part of the next GDPCR or GDN licence review. We sought views on this.

Responses

Some respondents considered that services currently provided by NGGD may reduce over the price control period. One respondent highlighted that xoserve costs are regularly reviewed by GDNs to ensure efficiency and another stated that xoserve may choose to in-source certain activities or seek alternative service providers. It was accepted by responses that it was likely that NGGD would continue to provide some of these services within the next few years.

Some respondents considered that including these services within SC E18 would be preferable. While there was also concern from others over the impact this would have on the current price control, the details supporting this view was not provided. Other respondents supported extending the consents to the end of the current price control period.

One respondent had no preference on how these services are treated, other than that it was reasonable for them to be treated consistently with the other services.

Ofgem decision

We consider that where it is probable that the need for consents is likely to continue for an extended period, we do not believe it efficient to continue to renew consents on an annual basis. Further, we do not support altering the scope of excluded services mid-way through a price control period unless there are compelling reasons to do so.

We consider that it is preferable to establish at the next price control review whether the revenue received from providing services under the xoserve General Services Agreement or similar should be treated as excluded services under SC E18.

We have therefore decided to extend the consent until 31 March 2013 (being the end of the current 2008-2013 gas distribution price control).

Agreement for the provision of call handling services - consent under SSC A36 (Restriction on Activity & Financial Ring fencing)

Under the Agreement for the provision of call handling services, NGGD provides a service for operating a call handling facility for the national emergency phone number. The agreement meets the current Gas Safety Management Regulations (GSMR) requirement that there should be a single national telephone number for reporting all natural gas emergencies.

Our initial view was that GSMRs do not exclude the possibility of GDNs running separate call centres with calls channelled through a single number. We invited views as to whether the technical challenges of call-channelling can be overcome and whether GDNs would be interested in providing this service independently. If the existing arrangement is to be maintained, we invited views on how the costs of this service should be treated.

Responses

Three respondents said they would prefer to retain the current arrangements at least until the next price control and that to change it would be less efficient and require additional resources to run additional call centres.

One of these respondents felt that the Gas Safety (Management) Regulations 1996 requires NGGD to provide a national gas emergency phone number and therefore the costs of the service should be included in National Grid's price control, possibly in transmission, with the costs being passed through for independent distribution networks.

Another respondent considered that it was possible to overcome the technical challenges of call-handling being undertaken by individual GDNs if economics and other considerations justify it, providing an enduring reciprocal agreement between the relevant parties could ensure that any misdirected calls are dealt with appropriately.

Another respondent considered that if the current arrangements were to be changed, care would need to be taken to avoid confusion of customers. They felt it would be appropriate to either grant consent until March 2013 and review this during the price control or alternatively include the activity as a permitted purpose.

Ofgem decision

There appears to be little support for running separate call centres to manage the 0800 gas emergency service. The technical challenges, necessary potential back up facilities and interrelations mean this may not be the most efficient solution. Additionally, since this

service is a vital part of the GDNs' safety cases, any changes would need to be accepted by the HSE.

We have therefore decided to extend the consent until 31 March 2013 (being the end of the current 2008-2013 gas distribution price control).

SOMSA arrangements - consent under SSC A36 (Restriction on Activity & Financial Ring fencing) and SSC A27 (Disposal of Assets)

The 19 December 2008 consultation letter stated that NGGD provided area control centre services to other GDNs for a transitional period after gas distribution network sales under SOMSA. These activities required consents to be granted to both NGGD (under SSC A36) and GDNs (under SSC A27). At the time of the consultation, it was anticipated that when the relevant consents expired on 30 October 2009 and 31 March 2009 respectively, the GDNs would be operating their control centres wholly and fully independently of NGGD.

In October 2009, NGGD confirmed that although all the GDNs had indeed established their own control centres and were operationally independent of NGGD, due to delays in the delivery of new supporting systems, the GDNs remain reliant on NGGD's Supervisory Control and Data Acquisition ("SCADA") and related systems (GTMS, SC2004 and telemetry) to operate their networks. NGGD stated that they will continue to provide some of the services contained within the SOMSA arrangements to GDNs. The GDNs have confirmed this to be the case. NGGD and the GDNs have stated that it was unlikely that these issues would be resolved before the end of March 2013.

Following further discussions with Ofgem, on 26 October 2009 NGGD requested that an extension to their SSC A36 consent relating to SOMSA be granted at least until the end of the gas distribution price control period.

In subsequent discussions with Ofgem, the GDNs have confirmed that in their view, they have each achieved full and independent control of their system operations and therefore they do not consider that an extension to each of their consents under SSC A27 (Disposal of Assets), which expired on 31 March 2009, is necessary.

Ofgem's decision

The SOMSA arrangements were intended to be temporary until the GDNs were able to fully and independently manage their control systems. We therefore consider that it is appropriate that any further consent that relates to SOMSA should be granted to allow only those activities that are still necessary for safe system operation.

We have therefore decided to grant limited consent in respect of SOMSA to NGGD until 31 March 2013 (the end of the current 2008-2013 gas distribution price control). However in making this decision, we are mindful that the further extension of this arrangement may delay the realisation of the full benefits of the sale of the gas distribution networks.

The Authority therefore reserves the right to seek to establish whether the SOMSA programme has been effectively managed and if regulated costs were efficiently incurred. We may consider at subsequent price control reviews whether that incurred expenditure was inefficient and, if so, whether to disallow all (or part) of it as appropriate.

Services that NGGT provides to GDNs

Agreement for the provision of transmission services - consent under SSC A36 (Restriction on Activity & Financial Ring fencing) and SSC A39 (Indebtedness)

Under this agreement, NGGT provides a number of services to the GDNs including emergency pipeline services, aerial surveillance services, live pipeline inspection services and specialist pipeline services.

Our initial view was that, whilst there is currently nothing to stop other companies from providing these services individually, the fact that NGGT sells the services as a bundle may make it harder for these companies to enter the market for individual services. At the same time we recognise that bundling of the services may result in efficiency savings that benefit customers. We sought views as to whether NGGT should be required to charge transmission services separately, or whether the status quo should be maintained.

Responses

One respondent proposed that the status quo should be maintained because other companies can also provide these services.

One respondent said that NGGT should offer these services individually to enable new entrants into the market but that GDNs would expect to benefit from efficiencies if more than one service is provided. The respondent could not see any reason why the service should not be treated as a permitted purpose.

Another respondent felt that it would not be easy or cost effective for certain emergency pipeline service facilities to be provided by individual GDNs. Some elements could be sourced elsewhere but the costs would be likely to be higher. The respondent favoured a longer term agreement with NGGT but felt short consent periods restricted this, so considered this service should be an excluded service. That respondent felt there was no impact on competition because alternative service providers were available.

Another respondent agreed that these services could be provided by other companies and that GDNs can tender on a bundled or unbundled basis. The respondent said that if NGGT did not provide the services, this would result in additional costs to GDNs. That respondent supported extending the consent until at least the next price control review to allow proper consultation and consideration of the cost implications.

NGGT stated in their consent application that these services are not offered bundled but as individual services, each being priced in a cost reflective way. NGGT supported extending the consents to the end of the current transmission price control to allow revenue from these activities to be excluded from de minimis revenue thresholds.

We did not receive any responses expressing concern over the distortion or restriction of competition.

Ofgem decision

It appears to us that NGGT provide these individual services priced on a cost reflective basis and that GDNs support the continued provision of these services. Respondents felt users have the option to choose alternative service providers for some or all of their needs.

We think that where there is a likelihood that the need for consents is likely to continue for an extended period; we do not consider it efficient to continue to renew consents on an annual basis. We do not support altering the scope of excluded services mid-way through a price control period unless there are compelling reasons to do so.

We have therefore decided to extend the NGGT SSC A36 and A39 consents until 31 March 2013 which aligns with the end of both the extended current transmission price control³ and the current gas distribution price control.

³ On 21 December 2009, we published a notification setting out the Authority's decision to implement a one year adapted roll-over of the current gas and electricity transmission price control (TPCR4) for the period from 1 April 2012 to 31 March 2013. This notification can be found here:
http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?file=Tp5%20rollover_12_2009%20sc.pdf&refer=Media/PressRel