

Response to consultation on the review of xoserve

We welcome Ofgem's review of the funding and governance arrangements of Xoserve. Xoserve, as the agent of the gas transporters, performs a vital role that underpins the successful functioning of the competitive gas shipping and supply market.

It is therefore in the ultimate interests of gas consumers that Xoserve operate in as optimal manner as possible. We recognise and agree with the concerns raised by CEPA in their report and believe that some of their recommendations for change would make a significant improvement to the current situation, particularly the Option C that they present.

Our responses to the questions raised in the consultation:

1. Xoserve's performance: What, if any, concerns do you have with regard to the performance of Xoserve? Do you agree or disagree with CEPA's articulation of network users' concerns about the responsiveness of Xoserve to industry change, and lack of transparency (pp.28-29)? Please provide reasons.

Yes we agree with the findings of the CEPA report. We have consistently found that the performance of Xoserve has not been what we expected or were led to be believed would be the case at its creation.

This failing in performance would seem to be a direct result of the funding and governance arrangements of Xoserve rather than any particular failing in the personnel employed within the organisation.

We have consistently articulated our concerns with regard to this situation to Ofgem, the Gas Distribution Networks (GDN) and Xoserve so are pleased to see that these are vindicated by CEPA in its report.

The CEPA report highlights the critical issues for us of lack of transparency with regards to Xoserve costs and their responsiveness to industry change (the lack of progress on resolving issues with regard to IGT customers is a good example of this).

2. Current arrangements: What concerns, if any, do you have with the current funding, governance and ownership arrangements? Do you agree or disagree with CEPA's assessment of the limitations of the current arrangements for Xoserve (pp.29-32)? Please provide reasons.

Yes we agree with the findings of the CEPA report.

Xoserve is a data service provision company and therefore not suited to a 5 or 8 year regulatory price cap mechanism aimed at incentivising efficiencies from gas network operators.

The value of Xoserve within the price control discussions (less than 0.5%) ensures that the issue is not prioritised as part of the negotiation between Ofgem and GDNs and appropriate regulatory scrutiny is not applied.

The governance model for xoserve is therefore flawed in that it provides only incentives for the GDN to minimise costs that their agent incurs. This may be sufficient to drive efficiencies initially but it does not provide the appropriate incentives to deliver any changes or improvements to services to help enhance competition in supply or shipping for the benefit of customers. This flaw in the governance model is key to the issues that affect Xoserve's performance.

With the impending implementation of the DCC and smart meters the retail energy supply market is going to go through a period of unprecedented change over the coming decade. It is vital that Xoserve be appropriately incentivised to respond to this change. Therefore a change to its governance arrangements are needed now as part of the current price control discussions.

3. Options for change: What are your views on the costs and benefits of the three options for change (Chs. 7)? Do you agree or disagree with CEPA's assessment of the options (Ch 8)? Are there any other options not identified by CEPA that we should consider?

A continuation of the existing governance arrangements for Xoserve will not allow for its current issues to be resolved.

Option A would seem to perpetuate the inappropriate incentives for inaction, would not resolve the issues around transparency of costs and leave the GDN to determine the priority for changes within the retail gas market rather than suppliers and shippers.

Options B and Options C would seem similar in concept and the benefits that they provide. The key difference between the Option B and C would seem to be who makes the initial decision with regard to Xoserve's priorities and funding.

In Option C these decisions would be made by the customers, or users, of Xoserve's services. We believe that these parties are best placed to understand what they need from Xoserve, to prioritise their workload and determine how investment should be spent. This model would provide a right of challenge by any funding party with Ofgem as ultimate arbitrator.

In Option B these judgements will lie with Ofgem who would consult (either via industry code modification processes or directly) with relevant stakeholders but ultimately would make decisions based upon a belief about what outcomes would be best for the market and for consumers.

This option is similar to the model DECC have adopted for the governance of the DCC service provider for smart meters. The justifications and logic put forward in the decision documents from DECC regarding the DCC equally apply to Option B of CEPA suggestions for Xoserve. To some extent the development and introduction of the DCC licence potentially answers many of the implementation concerns around a separate licensable activity for Xoserve's services that are raised by Ofgem. However we continue to believe that a preferable outcome would be the adoption of Option C.

4. Critical issues: What are your views on the critical issues identified by CEPA for determining the preferred option (p.73)? Are there any other critical issues we should take into account before making our decision?

The issues identified by CEPA do appear to be the pertinent questions to ask. Our views on these are as follows:

Are Xoserve's activities inseparable from the transportation businesses of the GDN? – Yes, Xoserve's function is to deliver the services that the transporters are obliged to perform for shippers within their licence. It does not perform any functions that the GDN could not undertake themselves internally. Evidence of this comes from the fact that IGT transportation businesses exist today, supplying almost 1 million consumers, without having to use Xoserve.

Are Xoserve's functions co-operative by nature? – Yes, the logic in establishing xoserve was to ensure that services that underpin the competitive gas shipping and supply market are undertaken by a single entity and provided in a common manner.

Is change too great a risk at this time? – Potentially, the gas supply and shipping market is undergoing a period of significant change. Of key concern are:

- a) Smart metering systems are expected to be rolled out over the remainder of the decade to all consumers changing significantly the amount of data that is available within the industry.
- b) DECC has already mandated that the responsibility for undertaking the central gas supply registration services for the industry will move from Xoserve and the GDN to the DCC in 2016/7.
- c) Xoserve is currently undertaking a significant programme to replace a significant number of its IT systems.

However a change to the funding and governance arrangements for Xoserve should not affect the operation of its business. In fact it can be argued reforming the governance and funding arrangements for Xoserve is needed to ensure that it can properly meet the challenges that are coming to it during the course of this decade.

5. Should we change the current arrangements? If so, what is your preferred option?

Yes and our preference would be for Option C which provides for a contractual arrangement for the industry to choose the service provider it wants to fulfil its requirements. We believe that this best aligns the decisions with regard to how central systems in the gas industry develop with the users of those services. We believe that this would lead to a lower cost solution for the industry and consumers than either of the other options. It would also allow services to evolve in a more responsive manner than either of the other options.

It removes the unnecessary involvement of the GDN in the decision making, freeing them to concentrate on their core business activities, and allows Xoserve to answer directly to the users of its services.



Concerns around mitigating excessive control by one or more users of Xoserve services at the expense of others are simply questions around the detail of the future governance arrangement and do not affect the underlying benefits that Option C offers.

Option B potentially offers many of the benefits of Option C but would require more regulatory input. In this option it would ultimately be Ofgem, in awarding and enforcing the Xoserve licence, which would be accountable for performance management. Many of the benefits of transparency and engagement with system change would equally apply to Option B as well as our preferred Option C.

Should Ofgem decide to pursue Option B we would envisage the initial licence for Xoserve being awarded for a fixed duration of time (potentially 10 years as is currently being suggested for the DCC). Without the realistic potential for losing its licence to operate there would be a real risk that Xoserve may not be sufficiently incentivised to deliver an acceptable level of service.

We do not support the adoption of Option A. This would seem to rely on an extension of the existing flawed User Pays arrangements with a mechanism of GDN and shippers agreeing the level of funding and prioritisation of work. This would perpetuate the difficult discussions which have been associated with potential changes to the gas industry under User Pays and it would be very difficult to see any resolution not requiring regulatory intervention and arbitration.

This process would risk delaying industry reforms planned for the benefit of the competitive retail market and consumers and would over the 8 years of the next price control take more effort for Ofgem than implementing either Options B or C.