

To: National Gas Transmission plc

Email: gas.systems@ofgem.gov.uk

Date: 14 August 2024

Approval of National Gas Transmission plc's request for a Derogation from Part C - Special Condition 9.19.11(b) of its Gas Transporter Licence

We¹ write further to National Gas Transmission's (NGT) letter to Ofgem, dated 22 February 2023, requesting a derogation in respect of Special Condition 9.19.11(b) of NGT's Gas Transporter Licence (the Licence)² in relation to compliance with the System Management Principles Statement (SMPS)³ for the Regulatory Years 2021-2022, 2022-2023 and 2023-2024. In that letter, NGT requested to replace the Independent Examiner's opinion with an Agreed Upon Procedures (AUP) report.⁴ This AUP report forms part of the Independent Examiner's statement that it has carried out an investigation into NGT's compliance with the SMPS, as required by Special Condition 9.19.11(a).

In our previous letter dated 5 October 2023,⁵ we approved the use of the AUP report and granted the requested derogation for the Regulatory Years 2021-2022, 2022-2023 and 2023-2024 only. This letter sets out our further approval of the derogation for Regulatory Year 2020-2021. The direction, which appears annexed to this letter, will give effect to this derogation (subject to the conditions specified therein).

¹ References to the "Authority", "Ofgem", "we" and "our" are used interchangeably in this document to refer to GEMA, the Gas and Electricity Markets Authority. The Office of Gas and Electricity Markets (Ofgem) supports GEMA in its day-to-day work. This decision is made by or on behalf of GEMA.

² National Grid Gas plc, Gas Transporter Licence, Special Conditions:
<https://epr.ofgem.gov.uk/Content/Documents/National%20Grid%20Gas%20Plc%20-%20Special%20Conditions%20Consolidated%20-%20Current%20Version.pdf>

³ SMPS: <https://www.nationalgas.com/about-us/how-were-regulated/gas-industry-compliance>

⁴ An Agreed Upon Procedures (AUP) report is a written factual report of findings from an auditor's testing and review of certain compliance standards. These tests and reviews are agreed in advance between the auditor and its client (in this case, NGT). The report is to contain the procedures to be performed (as agreed by the auditor and NGT), the associated work performed and the factual findings of the work performed.

⁵ See: [Approval of NGT's request for a Derogation from Part C - Special Condition 9.19.11\(b\) of its Gas Transporter Licence \(ofgem.gov.uk\)](#)

Background

The SMPS outlines which System Management Services (SMS) NGT will use to ensure the safe, efficient and economical operation of the National Transmission System (NTS). Part C of Special Condition 9.19 in the Licence sets out the requirements and processes NGT must follow in submitting and reviewing the SMPS. Every year, NGT must prepare a report detailing how it has complied with the SMPS. Accompanying this report, NGT must comply with Special Condition 9.19.11, which currently states:

“The report must be accompanied by a statement from an Independent Examiner that:

- a) confirms that the Independent Examiner has carried out an investigation, the scope and objectives of which were established by the licensee and approved by the Authority; and
- b) (b) gives the Independent Examiner's opinion on the extent to which the licensee has complied with the provisions of the System Management Principles Statement.”

Derogation request

NGT's auditor, assigned as the Independent Examiner, can no longer provide an assurance opinion due to stricter auditing practices from audit regulatory bodies. NGT's auditor has proposed an AUP approach as an alternative to giving a formal opinion. Under AUP, NGT and the auditor would jointly agree on a testing process to be carried out. The auditor would carry out these tests and issue an AUP assurance report summarising the completed tests and the results for each.

In accordance with Special Condition 9.19.28 of its Licence, NGT requested a derogation in respect of Special Condition 9.19.11(b) to allow the Independent Examiner to submit an AUP report instead of a formal opinion, which we approved for the Regulatory Years 2021-2022, 2022-2023 and 2023-2024 in our previous decision. This AUP report will form part of the Independent Examiner's statement that it has carried out an investigation into NGT's compliance with the SMPS, as required by Special Condition 9.19.11(a) of the Licence.

Our decision

Further to our previous review and decision, in which we granted a derogation for the Regulatory Years 2021-2022, 2022-2023 and 2023-2024, we are providing a further derogation covering Regulatory Year 2020-2021, in accordance with Special Condition 9.19.28 of the Licence.

We had not previously included the Regulatory Year 2020–2021 in our previous derogation as we considered that there was an unexplained and potentially unreasonable delay in NGT submitting its derogation request after the close of the relevant financial year year. We have since sought further information and have concluded that that there were extenuating circumstances which prevented NGT from submitting the request sooner.

Specifically, unexpected and unavoidable changes to external audit standards, and a need for NGT to engage with audit providers to workshop solutions led to an inability to comply in-year with existing requirements. There were also differing interpretations regarding timing requirements for seeking a derogation. The Licence does not currently specify a particular date for the submission of a derogation request, only that it must be done, “As soon as reasonably practicable after the end of each Regulatory Year”.

We would not usually consider these reasons sufficient cause to delay seeking a derogation; however, we must also consider the additional administrative burden and complexity brought about by the COVID-19 pandemic, in particular the impact of staff absences and operational disruptions.

In light of the above, we recognise that the early engagement that would normally be expected was not possible, and therefore we are satisfied that a derogation is appropriate in these circumstances.

The direction, which is issued in the Annex to this letter, will give effect to the derogation decision. This letter constitutes notice for the purpose of Section 38A of the Gas Act 1986 of the Authority’s reasons for its decision to grant the derogation by direction.

For 2024-2025 onwards, we will work with NGT to determine and implement a new assurance method which resolves any ambiguities in the current process, and which will be formalised as part of a broader Licence change in the near future.

William Duff

Head of Gas Systems and Operations

For and on behalf of the Gas and Electricity Markets Authority

ANNEX - Direction Notice

To: The Company Secretary, National Gas Transmission plc

Derogation by Direction issued to National Gas Transmission plc by the Gas and Electricity Markets Authority pursuant to paragraph 9.19.28 of Special Condition 9.19 Part C of the Gas Transporter Licence in respect of the System Management Principles Statement.

1. This derogation by Direction is issued by the Gas and Electricity Markets Authority (the "Authority") under paragraph 9.19.28 of Special Condition 9.19 Part C of the Gas Transporter Licence in respect of the NTS (the "Licence"), granted or treated as granted under section 7 of the Gas Act 1986 (the "Act") to National Gas Transmission plc (the "Licensee").
2. Paragraph 9.19.10 of Special Condition 9.19 provides that the Licensee, as soon as reasonably practicable after the end of each Regulatory Year, must prepare a report that:
 - (a) describes the manner in which, and the extent to which, the licensee has, during that year, complied with the provisions of the System Management Principles Statement; and
 - (b) states whether any modification should be made to that statement to reflect more closely the practice of the licensee
3. Paragraph 9.19.11 of Special Condition 9.19 provides that the Licensee's report must be accompanied by a statement from an Independent Examiner that:
 - (a) confirms that the Independent Examiner has carried out an investigation, the scope and objectives of which were established by the licensee and approved by the Authority; and
 - (b) gives the Independent Examiner's opinion on the extent to which the licensee has complied with the provisions of the System Management Principles Statement.
4. Paragraph 9.19.28 of Special Condition 9.19 provides that the Licensee may apply to the Authority for a derogation relieving the Licensee of any of its obligations under this condition.
5. The Authority grants the Licensee a derogation relieving the Licensee of its obligation under Special Condition 9.19.11 (b) to provide an Independent

Examiner's opinion on the extent to which the Licensee has complied with the provisions of the System Management Principles Statement, on the condition that instead the Licensee will provide an Agreed Upon Procedures Report by an Independent Examiner as set out in the Authority's Decision Letter dated 05 October 2023.

6. The considerations and reasons for the Authority's decision, in accordance with the Authority's duty under section 38A of the Act to give reasons, are set out in the Authority's decision letter to the Licensee, dated 05 October 2023.
7. The Direction shall cover Regulatory Year 2020-2021 only.
8. The Authority may revoke or vary this direction upon reasonable notice in writing to the Licensee.

Date: 14 August 2024

Signed for and on behalf of the Authority

William Duff

Head of Gas Systems and Operations

Authorised for that purpose by the Authority