

**Shell Gas Direct Limited**

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Dear Gill

**Ofgem Proposed Corporate Strategy 2003 – 2006**

I write in reference to Ofgem's proposed strategy. Shell Gas Direct (SGD) has a number of comments to make on the strategy and how Ofgem can prioritise its work. These comments reflect discussions at the seminar for licensees held on 30 January 2003.

**Priorities**

We consider that Ofgem should concentrate its resources on solving problems that consumers and suppliers have identified in the competitive market. A prudent approach should ensure that regulatory initiatives do not weaken the well-functioning competitive market and the potential for innovation driven by competitive activities by redirecting industry participant's scarce resources.

***Areas of higher priority***

One area that Ofgem has not focussed upon is LDZ interruptions regime. SGD has encountered difficulties in ensuring that we can get firm load for our consumers even with reasonable notice to Transco. We are aware that consumers have also raised concerns in this area (eg being declared a network sensitive load (NSL) by Transco; NSLs only occur on the LDZs). This should be considered before progressing with changes to NTS interruptions regime which appears to be working satisfactorily as it is.

As was mentioned at the Ofgem seminar, we note that Ofgem will be working on improving the customer transfer process. We hope that this will include work on transfers in the industrial and commercial market. There may be value in considering both of these markets together or it may be sensible, given the differences between the markets (eg with fixed versus rolling contracts; nomination procedures etc), to consider I&C issues as a separate, but related, stream of work.

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### *Areas of lower priority*

As set out above, we consider the NTS exit developments to be of a lesser priority although we recognise that requirements are now contained in Transco's licence. If this is to be carried forward, we would recommend that this is one area where the Authority gets a regulatory impact assessment on the full range of changes (network code, pricing, system management principles, procurement guidelines etc) before they give final approval.

We are not convinced that work on information in the gas market is required given the recent DTI report into gas prices which did not find any evidence of a problem in the market and in the absence of a clearly identified problem to resolve. We also question the advisability of the work on separate LDZ price controls given the potential for Transco to sell off one of the LDZs. We consider that it would be more effective, and less likely to cause difficulties in future, if the full scope of this happening were considered first. Parts that could be taken forward earlier (ie separate RPI-X controls) would then be developed within a robust framework taking account of potential future market developments.

### *Security of supply*

The term "security of supply" can appear to be used in different contexts. The Authority has duties in respect to security of supply as set out in the Utilities Act 2000. In respect of gas safety, the Authority must consult the Health and Safety Executive (HSE) while the HSE has its own, separate responsibilities in respect of gas safety in addition to those of the Authority. The Authority's duties to protect the public from dangers arising from the conveyance or use of gas are separate from its requirements in relation to longer term supply security including securing a diverse and viable long-term energy supply. It is important that these are not confused creating parallel and potentially conflicting work streams.

In regard to safety, the gas industry has been very active over the past few years through the Gas Industry Emergency Committee (GIEC). Ofgem, HSE, Transco, OTI, energywatch, UKOOA and the Gas Forum (representing suppliers and shippers through the Gas Industry Safety Group) all have membership of this group. It focuses on how to coordinate industry response to an emergency (eg from significant pipeline failure, major offshore failure, terrorist activities etc). GIEC has also considered how relighting domestic consumers can be carried out if in the unfortunate (and unlikely) event that an emergency results in large scale interruption of domestic consumers' premises. GIEC has also looked at commercial arrangements and is continuing to consider how to improve emergency contact information so Transco can quickly interrupt large, firm customers should an emergency be declared. We hope the Authority will concur with the view expressed by the HSE that a 'precautionary principle' should prevail in considering emergency arrangements.

Separately, the Joint Energy Security of Supply (JESS) group has been established by Ofgem and the DTI. We expect this group will focus on issues related to wider issues of long-term security of supply consistent with the Authority's duties in this area. GIEC and JESS need to ensure that their work programmes do not overlap and that both the short term interests of consumers in respect to safe supplies and consumers' longer term interests in respect of diverse and viable supplies are taken into account.

### ***Information issues and the upstream market***

We were surprised at **Callum McCarthy's** response to a query raised at the Ofgem seminar on 30 January 2003 regarding the wording in the **proposed corporate plan** to the effect that Ofgem will continue to work with the DTI to ensure that the offshore gas production industry encourages a competitive gas wholesale market. Mr McCarthy made reference to there having been an issue in respect to generators and intimated an undefined parallel with gas production. He also suggested, in reference to discussions on information issues, that we could meet with Ofgem staff to discuss further. Shell and UKOOA representatives have already met with Ofgem staff on several occasions regarding upstream information. Information has also been discussed extensively through a series of industry meetings. We are not convinced that further meetings will provide value to either party. We await Ofgem's response to the analysis and background on information flows provided so far by both the upstream and downstream industry. The offshore gas production industry continues to contribute to a competitive gas wholesale market.

### **Improving the way Ofgem works**

We welcome Mr McCarthy's statement that Ofgem will in future be doing a regulatory impact assessment (RIA) on major new initiatives. Robust RIAs should inform and improve Ofgem's decision making process and make a major contribution to Ofgem's communication of its policies. Further improvements should be considered for the rationale in Ofgem documents. It is essential to ensure that problems or market failures are clearly defined and clear evidence is provided (or if it is expected that a problem will arise in future, evidence for this should be given along with some analysis of its likelihood).

Ofgem has recently instituted quarterly meetings between shippers and the director of gas trading arrangements. We welcome this approach which has significantly improved communications between Ofgem and the shipper community.

The Authority should consider having specific targets for Ofgem staff regarding communications even if these targets are for internal use only. We assume that the Authority receives and considers information regarding the extent to which Ofgem is complying with the timescales provided for in its consultation policy document. We continue to recommend that a best practice document on consultation is produced in line with standards set by the Cabinet Office and other government departments building on the policy document. It is important that Ofgem can be seen to demonstrate that it has understood and responded fully to issues raised in responses to consultations rather than merely putting replies against each issue.

Ofgem should consider further the process it undertakes when making a decision and communicating it externally. Decision documents should be published before steps are taken towards implementation. On occasion, we have learned through indirect means that Ofgem was 'minded to' implement certain policies by certain dates as it had asked industry participants to take steps towards implementation. This was without any indication or explanation of why it was likely to come to the conclusions which would require this. Once a decision is made by Ofgem and published, sufficient time must be allowed to put the changes in place afterwards. This often means that several months or even a year will be required. Ofgem staff have suggested that we should prepare knowing the modification proposals are being considered. This approach cannot be consistent with Ofgem's requirements to promote efficiency. It is impossible to know which of the over 100 modification proposals made each year will be accepted by Ofgem and we trust that Ofgem staff will be considering our representations before

**final decisions** are made. It would also help if Ofgem could **make** its decisions in a timely manner. **In some cases, decisions** have **been expected** for over **six** months without any further explanation beyond ~~that~~ we should expect it **'soon'** being provided.

It appears that Ofgem has taken a decision to not send bound copies of its documents to **stakeholders** on request. **We find this very** disappointing and hope that this can be reconsidered.

**We** expect that with Ofgem's new **website** the diary of future activities and publications will be continually updated. Previously, there have been delays in updating the diary while **project plans have been** out of date. **We also** note that Ofgem published the **slides from** its **briefing** to City analysts but different areas were highlighted at the separate meetings could suggest another approach to its **plans**.

We assume that the **Authority** is **taking** steps to ensure that it is fully informed of major modifications **being proposed to the various** Codes and Ofgem's views upon these and the criteria upon which **decisions** are made. **We continue** to be concerned that decisions on modifications which can **have** significant, material impacts on our business are not **accorded** the same **level** of input from the Authority as other work by Ofgem staff. We would welcome fewer changes to the Network Code and consider that Ofgem can have a **major** impact on the number of **modifications** raised. In this **respect**, we were concerned to learn that Ofgem plans to introduce a requirement on NGC to raise **specific** modifications to the Connection and **Use** of System Code (CUSC). This **may introduce** further **conflicts in** Ofgem's role as it **will** be both the promoter of change **and make** the **ultimate** decision. **If it is considered necessary** to **take** this forward, the perception **of** conflict may possibly be reduced if final decisions were **made** by a full **meeting of** the **Authority**.

**We welcome the Authority's approach to having annual** meetings with stakeholders. However, it was **disappointing** that, **as with last year, the** Managing Director of Competition and Trading Arrangements **did not attend this meeting**. In addition, there was no one from her department at this year's meeting which was unfortunate as many of the questions raised were about **projects** being taken forward by the Trading Arrangements directorate. Also, **we** were not completely reassured that **all** members **of the Authority** were **fully briefed on all** aspects of regulatory change being promoted. We hope that all Managing Directors will **attend** next year.

**We would have also welcomed seeing all of** the Authority non-executive members at the meeting on 30 January 2003. The Authority makes **significant**, material decisions **which affect our** business particularly with the price controls and incentives for the monopoly **networks**. There is no opportunity for shippers and suppliers to meet with **the full Authority** to discuss the impacts on our own **businesses** in the competitive part of **the** market prior to final decisions being made. Suppliers and shippers' ability to subject these decisions to external **review** are lacking (**eg we cannot refer decisions on** monopoly operators' licences to the Competition Commission, only the licence holder and the **Authority can do this**). As we cannot require a meeting with the Authority to discuss the implications **of these decisions, these** annual **corporate plan** meetings remain **our** only opportunity to **discuss** issues **of** concern at **this level**.

### *Budget*

It would be helpful in **providing** data on the 3 year budget if Ofgem could provide some indication as to **the** extent to which increased **costs are** due to projected **salary increases** or **increases in staffing itself**. While we **note** that the budget is projected to **fall**, it would be more accurate to refer to the full costs, **without** rental income **etc, when**

considering cost trend (ie £40m for 2003/4, not £36m). Data from previous Ofgem plans indicated that OFFER and Ofgas separately (minus NETA or regional consumer offices) cost around £10m per annum less than Ofgem now does. While we recognise that more work is now being done on social and environmental issues, this does not completely explain the increase in costs given that Ofgem considers most of *the* market to be competitive and has withdrawn from price controls for all but the monopoly networks.

### Conclusion

Shell Gas Direct appreciates the developments that have been made by Ofgem in producing three-year plans. We also welcome the objective to improve the rationale section of publications to include a regulatory impact assessment. We have made comments in respect to priorities that Ofgem is adopting. We would welcome the opportunity to contribute to Ofgem's plans and projects.

Yours sincerely

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