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26<sup>th</sup> September 2003

Dear Kyran,

**Consultation Document: National Grid Transco – Potential sale of a Network  
Distribution Business**

Thank you for the opportunity to comment on the above consultation document. Statoil (UK) Ltd. (STUK) would like to make the following comments. STUK is responsible for the marketing of potential supplies of its parent company's Norwegian equity gas and the Norwegian State's equity gas in the UK market. Due to its size, proximity to Norway and its prospective gas supply shortfall in the next few years, the UK market is of great interest to us.

STUK are concerned that the potential impacts Transco's proposals could have upon the industry as a whole if this project was approved by the Authority in November. Our primary concern is that the information that has been provided has been set at a very high level preventing STUK from making informed decisions on the full implications that the sale of a Distribution Network (DN) by Transco would have on shippers, suppliers, Independent Gas Transporters and end consumers. As this project is of such magnitude, complexity and importance, STUK believes that the current timescales involved are inappropriate.

STUK do not believe that the proposed timescales are achievable and that the industry must first debate and discuss the right way forward in order to ensure that high costs, low levels of standards of service and fragmentation of the market does not occur by any process put in place to achieve the sale of a DN by Transco. This is of paramount importance and STUK would encourage Ofgem in ensuring that focus is not lost during the various stages of developing any reform.

As with any industry reform, it is in the interests of those participating in the market to become involved in ensuring that development/changes have been made to accommodate long term gain without incurring excessive costs. STUK believe that there are very few benefits to be gained by shippers, suppliers and end consumers in Transco selling its assets. The concern is that extra complexity in systems or processes would increase costs



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These would erode any benefit gained through efficiency generated by the independent distribution networks.

## Regulatory Architecture

The current UK gas market structure offers a stable platform for industry members under which, gas activities can be undertaken and also allows for improvements through either license changes or Network Code modifications. The industry has been operating under this regulatory framework for many years and STUK are concerned that changes made to the current market structure to the scale envisaged under these proposals would require major changes. STUK believe that any changes that are made to the governance arrangements should not only be workable but are also transparent in nature, uncomplicated, and provide the best option for the long term.

Under the various options listed by Ofgem for regulatory reform, STUK believe that full separation of the current GT license into Transmission (NTS) and Distribution licenses (Independent Distribution Networks - IDNs and Retained Distribution Networks - RDNs) would offer the best solution if Transco were able to sell a DN. However, this option would require careful planning in order to ensure that separation of these activities could be completed in an orderly manner without any conflict in roles occurring. This would also prevent any future ambiguity between the NTS and DNs. Under this approach, contractual relationships between the Transmission owner and the DN owner would need to be established in order to define how they would interact with each other on various services with identification from the onset as to the ownership of various data items. It is worth mentioning however, that this process is much more complicated than it first appears and that there is much work to be undertaken in ensuring that separation such as this can be completed successfully.

It may only be possible to ensure non-discrimination by Transco between IDN's and RDN by separating out the RDN's into a separate business unit under Transco both legally and financially independent from the transporter.

Combined transmission and distribution licenses may initially appear to be a feasible option, enabling little regulatory impact, lower associated costs and a shorter time for implementation. However, STUK are concerned that this option would only serve as a short-term solution and would prevent the clear definition of roles and responsibilities required in order to further develop the gas market.

With regards to the Network Code, STUK considers that separate Network Codes should be developed for both the NTS and the DNs (IDNs and RDNs). This would create a total of two Network Codes to which all shippers must become signatories. Again, for the same reasons identified above, this would create a structure that would work better for the longer term.

The consultation document mentions at a very high level the concept of the offtake agreement. STUK believe that such agreement must be fully discussed between the relevant parties to ensure that all areas are covered. We also believe that agreements such as these should be as generic as possible and that any specific issues could be incorporated into the schedules and appendices. The benefits of having generic agreements would ensure that Transco does not give preferential treatment to an RDN. In considering this matter, we would welcome Ofgem's comments on whether IGTs will be brought into the



new regulatory structure, and if not, on what basis are the IGTs being differentiated from DNs?

The following is by no means a definitive list of the issues and concerns that we have highlighted concerning proposals for the offtake agreement:

- The consultation document does not sufficiently detail the scope of the offtake agreement
- The offtake agreement must assign clear responsibilities for data ownership and standards of service levels e.g. who would be responsible for requests made by shippers for increases/decreases in SOQ capacity? This is currently the responsibility of the LDZs. Another example is who would be responsible for GT queries?
- Management processes must be clearly defined under such agreements with an auditing trail to ensure non-discriminatory behaviour
- Such agreements must detail arbitration procedures in the event of disputes e.g. balancing, SPA processes, meter readings
- Adjustment process must be included under these agreements e.g. NTS/DN elements involving invoicing

The sale of a DN by Transco should improve overall cost efficiencies. However it is difficult to comprehend how increasing the overall complexities within the regulatory framework can reduce costs. Once Ofgem completes a full and comprehensive Regulatory Impact Assessment (RIA), and the outcome demonstrates that the overall process is too complicated, then it would be necessary to question whether this programme of work should continue or not. It is not viable to continue with developing reform when the cost efficiencies of that reform will never be realised.

It is important to note that all of these proposed solutions represent increasing complexity in the governance structure of the gas industry. This complexity will not improve transparency in the relationship between transporter, distributor, shipper, supplier and customer (especially considering the variety of new agreements which may need to be created to formalize these arrangements). As such this increase in complexity could be viewed, as a barrier to entry, creating unwieldy or complex arrangements for a new entrant to gain access to the market cannot be the goal of this process.

### **Exit & Interruptions Regime**

STUK believes that under the existing regime, customers should be offered a greater level of choice for the interruption services that they offer to Transco. Customer representative groups have informed the industry that changes to the interruption regime should be minimised and that prices should remain simple. They have expressed a need to be able to receive a greater choice from Transco on interruptible services instead of the flat 45 days interruption that Transco currently requests from them.

STUK consider that the sale of a DN will only lead to adding an extra layer of complexity into either the current exit and interruption regime or the proposals that were being developed by the workstream members prior to Ofgem incorporating this into the DN sale project. By doing the latter, the industry faces many challenges, notably the increased number of parties being involved within any interruption being called at a DN level. This will lead to



developing both contractual relationships and communication links between the NTS, the eight DNs, shippers, suppliers and end consumers.

Ofgem have previously stated that the exit and interruption regime needed reform as it was claimed that there was evidence that firm sites were subsidising interruptible sites through the charging mechanism and that Transco were over contracting for the provision of interruption that was necessary to run a safe and efficient system. The workstream members requested further analysis of this from Ofgem in order to justify whether radical reform of the exit and interruption arrangements were required. We would request Ofgem to provide the industry with this information as soon as this is available.

## **Gas Balancing Regime**

STUK do not support the concept of multiple SOs for the purpose of gas balancing and believe that a single SO should govern the transmission and distribution networks. This is to ensure that trading can continue at the NBP without the market becoming fragmented and that liberalisation of the UK market is not destroyed.

The wholesale gas market functions well and changes being introduced to the gas balancing regime under this programme of work will not improve it.

## **Supply Point Administration (SPA)**

STUK believe that of paramount importance within the SPA is the stability of the Change of Supplier (CoS) process. Shippers and suppliers have developed their systems to ensure they comply with SPA rules under the Network Code. The problems currently encountered within SPA are primarily to do with data inaccuracies caused by Transco's inability to effectively manage the date items. We consider that the whole SPA process could be vastly improved by a greater focus placed on data quality by Transco and not necessarily for the industry to incur system costs through the re-engineering of the SPA processes.

Transco's proposals for an agency to undertake the SPA function causes us much concern, as we believe the agent proposal must be independent from Transco where shippers and suppliers are able to become involved in selecting the new service provider. An independent agent would ensure non-discrimination between services offered to IDNs and RDNs and would have SPA as its core function ensuring a higher level of service is offered with continued improvements being developed.

It is important to ascertain at this stage whether the data would be owned by the Agent, Transco or the DNs as concerns such as capacity issues, which are covered under SPA, would need to be resolved. Under such a scenario, it is important to understand how this will work in practice and who will need to take responsibility for this.

STUK are unclear how these proposals would be incorporated within the work undertaken so far on SPAA. What would the effects be if I&C suppliers, Transco and IGTs did not sign up to becoming members of SPAA? We are concerned about the number of individual projects currently being discussed within the industry and which need a coordinated approach being taken by Ofgem as many inter-link with one another, e.g. SPAA, RGMA,



Customer Transfer Process. There is a high risk that these projects will be developed in contradiction to the aims of the separation process.

## **Regulatory Impact Assessment (RIA)**

STUK do not consider it appropriate that a project of this scale can be allowed to proceed with only an initial RIA undertaken. We believe that Ofgem should conduct a full RIA openly and transparently before the Authority makes a decision. Ofgem should source information from as many industry members as possible. This should provide the industry with a detailed cost/benefit analysis where informed decisions can be made.

We also believe that a full RIA should be conducted and the details from this should be disclosed to the industry prior to the Authority making a decision in November. This ensures that the full benefits are realised prior to assent being given.

STUK find it difficult to comment on the accuracy of the current RIA, as the model used to construct the implied costs is too imprecise. It may prove more informative to establish the true extent of the changes required and the associated costs. This may give a clearer impression of what the benefits and costs of this proposal are.

## **Conclusions**

The Authority must only give its assent to any proposed sale once Transco can clearly demonstrate that it has met all of the gateway requirements. At this stage, we are unconvinced that the industry will benefit from any disposal of assets by Transco. Instead, we firmly believe that significant costs will be incurred together with increased risks from regulatory, financial and operational complexity.

STUK believe that the following must be taken into account when considering any proposed change:

- To try and maintain the existing processes and procedures
- To ensure there is uniformity of IT systems, pricing structures and gas operations across the entire network
- To integrate reform with projects which are currently under development (Gemini, Customer Transfer Programme, SPAA, RGMA, Exit & Interruption, Credit Arrangements)
- To maintain current market structure and avoid fragmentation of the NBP
- To avoid complexity which could create barriers to entry
- To ensure that a workable and least cost option is in place for the industry
- To ensure that reform benefits all end consumers

If approval were given by the Authority for Transco to proceed with the sale of a DN, STUK would like assurances from Ofgem that Transco will take a coordinated approach and avoid



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rushing through proposals. The industry needs to be fully informed of the impacts of this project beforehand so that we do not make changes without addressing all issues first.

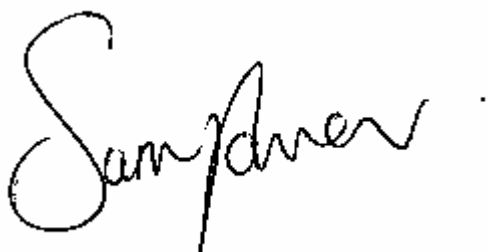
We agree with Ofgem's comments that pancaking of transportation charges could arise from the separation of DN and Transco pricing methodologies at the NTS and DN interface. This should ensure that there is no duplication of charging for capacity or services.

We would recommend that Ofgem undertake analysis of the likely costs and benefits of disposal from which elements of double counting are excluded, for example the benefits perceived from the separation of Transco's price controls. This will ensure that true costs and benefits are realised through the sale of a DN.

On a final point, STUK would like to know what assessment criteria will be used by Ofgem in measuring success for this project as this will provide the industry with clear signals on whether the industry has benefited from this major reform. It is important to establish now how end users or other participants will see these benefits returned to them and how Ofgem intend to assess the success of the changes.

STUK trust that our comments will be given due consideration and should you wish to discuss any aspects of this response further please contact me on the above number.

Yours sincerely,



Sam Parmar  
Regulatory Affairs Advisor



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