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Dear Richard

Quality of Service for Gas Distribution Networks – Initial Consultation

We welcome the opportunity to respond to the above consultation.

As illustrated by Ofgem in chapter two of the consultation document, we believe that the existing regulatory framework already provides for a significant number and range of quality of service incentives. Therefore, based on this assessment and to the extent that there is no evidence of detrimental non-performance, we believe that the existing incentive framework is sufficiently robust.

In any event, we believe that it is particularly important to restrict the setting of new, or amending existing performance incentives mid price control unless there is equal prospect of reward/penalty for the respective network owner. For example, in our view, it would be inappropriate to add to the suite of existing guaranteed standards of performance, or to increase the “penalty” associated with such standards mid price control on the grounds that it could represent a significant additional risk to a network owner that had not been accounted for at the time the price control was accepted.

Turning now to Transco’s obligations under Special Condition 36 and Ofgem’s intention to introduce an Information and Incentives Project (IIP) incentive scheme from April 2005. We believe that a considerable amount of detailed reporting and analysis is required in order to set appropriate targeted incentives for each Distribution Network (DN) that would deliver real benefits to customers. However, Transco has only been required to report disaggregated interruptions data from April 2003 and we do not believe therefore that there is sufficient information available to enable Ofgem and the industry to identify meaningful DN-specific incentives for next April. That is, we do not believe that the available data can be used with sufficient confidence to set a financial IIP incentive.

We therefore believe that it would be more appropriate to continue to gather and publish disaggregated data in accordance with Special Condition 36 with a view to introducing relevant DN-specific financial incentives at the beginning of the next price control (ie IIP

should remain a non-financial incentive). In doing so it will of course be necessary to consider the physical characteristics of each of the DNs separately. For example, when analysing interruption duration data, it will be necessary to take into account the physical and economic differences associated with rural networks when compared to those DNs that are predominantly urban.

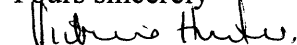
As you will be aware, NGT is currently considering the potential sale of one or more of its eight DNs. Clearly, in the event that a sale(s) does proceed the potential for regulatory and performance comparison in gas transportation services would be greatly enhanced to the benefit of customers. Therefore, rather than changing the existing quality of service incentives or introducing new incentives at this stage, we believe that it would be far more appropriate to maintain the existing framework for the remaining price control period while continuing to collate DN specific information from both Transco and the new DN owners. This approach would also enable new DN owners to be directly involved in the review and development of the quality of service incentives associated with their networks while ensuring that existing performance levels are maintained.

The above interaction of performance incentives and the DN sales process is particularly relevant when considering Ofgem's recent proposals for licenced governance of connection standards. We believe that it is inequitable for new DN owners to be burdened with complex standards in this area on account of Transco's historically poor performance. The presumption should be that new DN owners would not be subject to such standards unless, and until, a similar scale of poor performance with their provision of connection services is demonstrated.

In conclusion therefore, we do not believe that there are gaps or weaknesses in the existing framework of regulation for DNs in respect of delivering robust quality of service. In any event, as a point of principle, we do not believe that it is appropriate to alter the parameters of any existing incentive or to introduce a new incentive mid price control period. Although we recognise that it was Ofgem's intention to introduce an IIP-type incentive from April 2005, we are concerned that only one full year of disaggregated data is currently available. We therefore believe that it would be more appropriate to continue the reporting requirements under the RIGs for each DN with a view to introducing financial incentive parameters at the start of the next price control period. In any event, in recognition of the DN sales process, and to the extent that Ofgem does conclude that new or amended incentives are required, the framework should, in our view, contain a mechanism for a new DN owner to be exempted from any new standard; a cap on the overall liabilities arising from the new incentives in any one year; and a right of appeal for the affected DN owner.

Please do not hesitate to contact me if you would like to discuss any of the above in more detail.

Yours sincerely



Rob McDonald

Director of Regulation

