

National Grid Transco – Potential sale of gas distribution network businesses

Licensing: Next Steps

Formal consultation under Section 23 and informal consultation under Section 8AA of the Gas Act 1986

November 2004

Summary

This document sets out the next steps in the process for the proposed restructuring of Transco plc's (Transco's) six Gas Transporters (GT) licences¹. This restructuring is required in the event that National Grid Transco plc's (NGT's) proposed sale of one or more of its gas distribution network (DN) businesses proceeds. This document follows the publication in September 2004 of a consultation document setting out Ofgem's initial thoughts on the proposed restructuring of Transco's GT licences². This September document set out Ofgem's initial views on how Transco's GT licences should be modified and restructured to allow the proposed transaction to proceed whilst protecting the interests of customers.

In issuing this document and describing the proposed regulatory process to be followed it is important to make clear that there can be no expectation on the part of NGT, Transco, potential DN purchasers, shippers, suppliers, Independent Gas Transporters (IGTs) or any other interested party either as to what the Gas and Electricity Markets Authority's (the Authority) final decision in relation to the proposed transaction may be, or as to the regulatory framework which may be implemented if the Authority consents to the proposed transaction. The information contained in this document is not binding on the Authority. Nothing in this document is to be construed as granting any rights or imposing any obligations on the Authority. The Authority's discretion will not be fettered by any statements made in this document.

Since the publication of the September document, Ofgem has received extensive feedback from potential purchasers of DNs, shippers, consumer groups and other interested parties. Ofgem has also consulted on the key issues in industry workgroups.

A further development since the publication of the September document is that, on 5 November, Ofgem (without in any way fettering the Authority's discretion in relation to the proposed transaction) granted five additional GT licences to Transco plc, following its application (in connection with the proposed transaction) for additional GT licences in July. These licences currently substantially replicate Transco's original GT licence. Therefore, Transco currently has six virtually identical GT licences.

¹ Transco plc is a wholly owned subsidiary of National Grid Transco plc

² National Grid Transco – Potential sale of gas distribution network businesses, Initial thoughts on restructuring Transco plc's Gas Transporter Licences, Consultation document, September 2004 215/04

This next steps document sets out the next stage of the proposed licence restructuring process. There are two main parts to this restructuring process:

- ◆ **Part 1** is to initiate a formal consultation to modify each of Transco's six GT licences under Section 23 of the Gas Act 1986 (the Act). These licence modifications will be limited to the changes to conditions relating to Transco's price control and are designed only to separate the price controls between the six Transco GT licences. By separating the price control sections, each of Transco's six GT licences will apply to a separate part of its gas transportation business. In aggregate however, the overall level of the price control will be unchanged. Appended to this document is a redrafted version of the licence conditions that would change should the modifications proceed for each of Transco's six GT licences; and
- ◆ **Part 2** is to consult further, on an informal basis, on the substantive licence changes that would be required to support Transco's proposed divestment of its DN businesses so that customers' interests are protected. Ofgem considers that this will allow further time for consideration of these important issues, in light of respondents' views to its September document. It is intended that, eventually, these changes will be consulted upon formally as part of the 8AA process (with an associated additional section 23 modifications for those businesses that will continue to be owned by Transco), under which the Authority would consider whether to consent to the transfer of a number of the GT licences held by Transco to separate Transco owned subsidiaries. Also appended to this document is a revised draft version of a composite GT licence that reflects the proposals.

The main issues for each part of this document are discussed below.

Key issues for the Section 23 formal consultation

The intended effect of these proposed modifications would be to ensure that the overall current price control for Transco will not change; rather, that the price control conditions are split between the revenue restriction provisions in Transco's original

licence and each of the five new additional licences between National Transmission System (NTS) and DN activities.

The key issues with regard to the formal consultation process to adjust the price control terms of Transco's GT licences are:

- ◆ separation of DN and NTS licence conditions. Currently, Transco's price control licence conditions cover aspects of both the NTS and DN business within the same conditions. Hence, it has been necessary to separate the current obligations within each licence condition so that, for each business, only the relevant DN or NTS licence conditions apply; and
- ◆ differentiation of DN specific licence conditions. For some licence conditions, it has been necessary to separate out price control obligations that are within a single condition into DN specific licence obligations.

Currently all gas transportation assets owned by Transco are operated pursuant to the original Transco GT licence. As at the date of this document, the five additional Transco GT licences, whilst active, do not relate to any particular gas transportation assets owned or operated by Transco.

As part of the proposed transaction, the Authority proposes to modify each of the six Transco GT licences in the manner set out in the attached notice to separate the price controls and achieve revenue separation between Transco's NTS and each of the DNs which are proposed to be disposed of by Transco (IDNs) and each of those DNs which are proposed to be retained by Transco (RDNs). If the modifications proposed in the attached notice are made, each of the five additional Transco GT licences will relate to specific DN assets and the original Transco GT licence will relate to the NTS assets only.

As part of the proposed transaction, Transco is proposing to hive-down four of its DN businesses to four wholly owned Transco subsidiary companies. The proposed hive-down by Transco will require, *inter alia*, the consent of the Secretary of State for Trade and Industry (the Secretary of State) and the Authority pursuant to Amended Standard Condition 29 of the original Transco GT licence. It is expected that both the Secretary of State and the Authority will decide on this matter in mid January 2005. The proposed modifications to each of the six Transco GT licences which are set out in the attached notice would not be directed by the Authority in the event that Transco does not obtain

the consents necessary to undertake the hive-down of the DNs from Transco to the wholly owned Transco subsidiary companies.

In order to make the modifications set out in the attached notice to each of the Transco GT licences (i.e. the original Transco GT licence and each of the five additional Transco GT licences), Transco's consent will be required in accordance with the requirements of section 23(6) of the Act as it will be the holder of the relevant licences at the relevant time. This means that only Transco will be asked to provide consent to the proposed modifications. This consent, if provided by Transco, would enable the Authority, but not oblige it, to direct that the modifications be made.

However, in light of the proposed transaction, Ofgem would particularly hope to receive comments on the proposed modifications to the Transco GT Licences from, amongst others, potential DN purchasers and other interested parties.

Key issues for the Section 8AA informal consultation

The key issues raised as part of the informal consultation process are:

- ◆ the **structure of the licences**. Ofgem has proposed a licence condition (known as the "private CLM") that would apply to all of Transco's six GT licences that would effectively mimic the effects of the statutory CLM procedure contained in Section 23 of the Act. This would allow a range of NTS and DN GT licence conditions to be modified collectively across what are currently Transco's GT licences;
- ◆ the **governance arrangements**. The proposed sale of DNs will mean that additional licence obligations will need to be added to the six GT licences in respect to transportation charging and the Network Code.
For:
 - ◆ **transportation charges**. It is proposed that NTS and DN-GTs should use reasonable endeavours only to change their charges twice a year, namely on 1 April and 1 October. This is designed to mitigate the risk that network owners could change their charges frequently and in an uncoordinated manner which might impose additional costs upon users of the network. Also, to prevent uncoordinated changes in the methodology used by DN

owners to calculate the level of their charges to customers, it is proposed that a licence condition be placed on DNs so that the development and modification of DN charging methodologies be administered by a centralised governance entity; and for

- ◆ the **Network Code**. It is proposed that the licence condition that governs Transco's existing Network Code will include the commercial arrangements necessary to manage the interface between the NTS and DNs. This condition will provide for Short Form Codes (SFC) and an overarching Uniform Network Code (UNC) and set out the modifications process for each.
- ◆ **system security**. The document proposes a number of conditions in relation to **emergency services coordination** by the DNs. In particular, it is proposed by Ofgem that DNs be obliged to provide emergency services to the NTS and charge for this service at a reasonable rate. Ofgem has considered carefully all the representations made with respect to emergency service provision to Independent Gas Transporters (IGTs), which are the small independently owned networks currently connected to Transco's network. Ofgem considers that there should be no change to the current arrangements by which emergency services are provided to IGTs and that the current contract for provision of these services should continue as now. Any required changes to the current arrangements between IGTs and DNs are not, in Ofgem's view, connected to the potential sale of DNs. However, Ofgem is committing to undertake a full review of such services when the current commercial contract with Transco expires. On **pipeline security standards**, Ofgem considers that a continuation of the current standard, known as the 1 in 20 obligation, is appropriate for all GT networks.
- ◆ **price controls**. Consistent with its previous statements, Ofgem proposes not to reopen Transco's price controls, so that, overall, the amount of money recovered from customers by GTs will be the same over the remainder of the control period irrespective of whether the proposed sale of DNs proceeds. In addition to this, Ofgem is proposing that there should be an incentive scheme applying to DNs to encourage efficient investment decisions by network owners. These incentive arrangements

will be supplemental to the price control arrangements and will be considered in detail in a separate consultation document.

- ◆ **network service agreements (NSAs).** If the proposed sale of DNs were to proceed, Transco would put in place for an interim period a number of agreements between the new owners of the DNs and itself. One example of such agreements is the System Operator Managed Services Agreements (SOMSAs), under which Transco would provide the independent DNs (IDNs) with system operation services immediately following the sale. In the longer term, it is envisaged that the IDNs would undertake these activities for themselves. During the consultation process, some parties have suggested that these agreements should be regulated. However, Ofgem is of the view that this should not be the case. Rather, it has defined the responsibilities of each network owner and believes it is for that owner to determine the best way of discharging those responsibilities.
- ◆ **standards of performance.** While not a licence obligation, currently Transco conducts satisfaction surveys of its DN customers that have had their supply of gas interrupted (both for planned reasons relating to maintenance of pipelines and unplanned). To ensure that there is no reduction in the level of this monitoring, Ofgem proposes to place an obligation on all DN-GTs to continue surveying customers that have had their gas supply interrupted. There will be no revenue implications attached to this obligation. On connections, Ofgem intends to place licence obligations on all GT licensees to ensure that the current obligations that are currently placed upon Transco with regard to standards of performance in relation to connections continue to apply.
- ◆ **business separation.** The document also highlights Ofgem's proposals with respect to separation of a DN's business activities from any competitive activities it may have. It also sets out proposals for arrangements to ensure that there is no undue discrimination between NTS and RDN businesses.

Way Forward

Ofgem invites views on all of the issues raised in this document. For the:

- ◆ formal consultation on the proposed section 23 modifications to Transco's price control in each of its six GT licences, Ofgem requests that views from respondents are submitted by 23 December 2004; and for the
- ◆ informal consultation on the section 8AA modifications, Ofgem requests that respondents submit their views on the issues raised in this document by the 7 January 2005. Ofgem would particularly welcome an early response on these issues from NGT and potential purchasers, and ideally by 23 December 2004.

Currently, the Authority is intending to consider whether to consent to Transco's proposed disposal of DN assets in mid January. If the Authority decides to grant this consent, Ofgem will, shortly afterwards, and subject to the responses received to the section 23 formal consultation in this document, undertake the modifications to the price control licence conditions. The subsequent Section 8AA modifications being discussed and informally consulted upon in this document will be the subject of a further consultation document that is intended to be issued in the middle of February 2005.

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1. Introduction

Purpose of this document

- 1.1. Following NGT's³ announcement, in May 2003, that it would consider the sale of one or more of its gas Distribution Networks (DNs), Ofgem initiated a programme of work⁴ to explore the potential costs and benefits that such a transaction may have for consumers. Any sale of DN assets by NGT would require the consent of the Gas and Electricity Markets Authority (the Authority), the Health and Safety Executive (HSE) and the Secretary of State for Trade and Industry (the Secretary of State).
- 1.2. As part of this process, in September 2004⁵ Ofgem issued its initial analysis of the modifications to the gas transporter (GT) licence (the 'September document'), in terms of both content and structure, that would be required to ensure that the regulatory framework to support a divested industry structure is in place in the event of DN sales so that customers are protected.⁶
- 1.3. The purpose of this document is to set out respondents' views to its September document, and Ofgem's revised proposals in light of these views. The document also sets out the next steps and invites views on both:
 - ◆ the formal Section 23 notice; and
 - ◆ the informal consultation on the licence modifications which will occur at the Section 8AA stage (along with the associated Section 23 notice at that time) should the Authority grant its conditional consent to DN Sales in January.
- 1.4. As this proposed transaction is not a regulatory initiative but a commercial transaction by NGT, Ofgem intends only to modify those GT licences currently held by Transco plc and not any other GT licences. However in identifying the

³ Transco plc is a wholly owned subsidiary of National Grid Transco plc.

⁴ Appendix 1 gives details of Ofgem's regulatory process associated with NGT's proposed DN sales. This includes a timeline of the commercial transaction and the associated regulatory process.

⁵ National Grid Transco – Potential Sale of gas distribution network businesses, Initial thoughts on restructuring Transco plc's Gas Transporter Licences, Consultation document, September 2004 215/04.

⁶ Notice under section 7B(9)(c) of the Gas Act 1986 of the grant of five new additional gas transporter

proposed modifications, Ofgem has given careful consideration to the impact on other GTs and in particular has satisfied itself that no undue discrimination would be created through the proposals set out in this document. However, if any respondent considers that any proposals would adversely impact upon them, Ofgem would welcome representations on this matter.

- 1.5. In issuing this document and describing the proposed regulatory process to be followed, it is important to make clear that there can be no expectation on the part of NGT, Transco's potential DN purchasers, shippers, suppliers, Independent Gas Transporters (IGTs) or any other interested party either as to what the Authority's final decision in relation to the proposed transaction may be, or as to the regulatory framework which may be implemented if the Authority consents to the proposed transaction. The information contained in this document is not binding on the Authority. Nothing in this document is to be construed as granting any rights or imposing any obligations on the Authority. The Authority's discretion will not be fettered by any statements made in this document.

Background

- 1.6. The September document gave a high level outline of the issues surrounding each licence condition and Ofgem's initial view of the proposed revised licence structure. The document also gave Ofgem's initial views of the proposed changes that would be required to each licence condition (including potential new licence conditions) to support a divested industry structure in the event that any DN Sale were to occur.
- 1.7. The document explained that it was Ofgem's intention to modify the GT licences⁷ held by Transco plc at three separate stages:
- ◆ the Section 23 notice (attached as an appendix to this document);
 - ◆ the Section 8AA consent; and

licences. This document is available on the Gas Distribution Network Sale page of Ofgem's website.

⁷ Transco plc was issued with 5 mirrored GT licences on 5 November 2004, following its request for additional licences in July 2004 as part of the DN sales process.

- ◆ as part of any consent to the disposal of relevant DN assets under Amended Standard Condition 29 (Disposal of Assets) of Transco's original GT licence.

1.8. The background to this document is set out in full in Chapter 2 of this document.

Respondents' views

- 1.9. In total Ofgem received twenty responses to the initial consultation document. These respondents included Transco plc (the licensee), all four potential purchasers, independent gas transporters (IGTs), shippers, suppliers, the Gas Industry Safety Group (GISG), energywatch and other interested parties. Three responses were confidential. All other responses can be found on the Ofgem website (www.ofgem.gov.uk).
- 1.10. Ofgem would note that three of the responses provided were identical responses from companies within the same group. These responses have been treated as a single response for the purposes of the respondents' views summaries provided within this document.

Structure of this document

- 1.11. This document is structured as follows:
- ◆ Chapter 2 sets out the background including the regulatory framework that is relevant to the proposed amendments to Transco plc's GT licence;
 - ◆ Chapter 3 explains the Section 23 notice and associated formal consultation;
 - ◆ Chapter 4, Chapter 5 and Chapter 6 consider the changes that will be necessary as part of the Section 8AA process (and associated Section 23 notice):
 - ◆ Chapter 4 sets out the key issues from respondents' views to the September document and sets out the way forward on each of these issues;

- ◆ Chapter 5 gives respondents' views and the way forward for each of Transco plc's existing licence conditions;
- ◆ Chapter 6 gives respondents' views and the way forward for each of the proposed new licence conditions. This chapter also identifies where new licence conditions have been identified since the September document; and
- ◆ Chapter 7 explains the proposed way forward.

1.12. In addition, there are a number of appendices (which have been published separately in conjunction with this consultation document). These are:

- ◆ Appendix 1 – DN sales timeline;
- ◆ Appendix 2 – List of respondents to the September document;
- ◆ Appendix 3 – Proposed treatment of licence conditions;
- ◆ Appendix 4 – DISG 19 minutes;
- ◆ Appendix 5 – Section 23 notice;
- ◆ Appendix 6 – Section 8AA mapping tables;
- ◆ Appendix 7A – Designated Standard Conditions;
- ◆ Appendix 7B – Composite Standard Special and Special Conditions; and
- ◆ Appendix 8 – Section 23 Proposed Revenue Restriction Definitions.

Views invited

1.13. Ofgem invites views on all of the issues raised in this document. For the:

- ◆ formal consultation on the section 23 modification to Transco's price control, Ofgem requests that views from respondents are submitted by 23 December 2004; and for the
- ◆ informal consultation on the section 8AA modifications, Ofgem requests that respondents submit their views on the issues raised in this document

by 7 January 2005. Ofgem would particularly welcome an early response on these issues from NGT and potential purchasers, and ideally by 23 December 2004

- 1.14. Respondents are requested to provide views in a timely manner. Responses should be addressed to:

Sonia Brown

Director, Transportation

Office of Gas and Electricity Markets

9 Millbank

London SW1P 3GE

(Telephone 020 7901 7412)

Electronic responses may be sent to tracey.hunt@ofgem.gov.uk

- 1.15. Respondents are requested, as far as possible, to provide non-confidential responses. Ofgem would also prefer for non-confidential responses to be sent electronically so that they can be placed on the Ofgem website. Respondents are free to mark their reply as confidential if they wish.
- 1.16. If you wish to discuss any aspect of this paper please do not hesitate to contact Helen Connolly (telephone 020 7901 7267) who would be pleased to help.

Way forward

- 1.17. Ofgem will carefully consider all responses received to this consultation document. Discussions on the drafting of specific licence conditions will continue through the Development and Implementation Steering Group (DISG).
- 1.18. If in January, the Authority grants its consent to the disposal of DN assets, and subject to respondents' views to this consultation document and the attached Section 23 notice, Ofgem expects to direct the proposed modifications set out in the Section 23 notice.

- 1.19. In January Ofgem also envisages publishing on its website and discussing with the DISG final drafts of the licence conditions due to be modified at the Section 8AA stage (including the associated Section 23 notice). It is planned, if the Authority gives its consent, that the Section 8AA (and associated Section 23 notice) consultation will commence in February 2005.
- 1.20. This document therefore represents the next step in the process towards developing a proposed licence structure which would ensure that the interests of customers are protected in a divested industry structure post any DN Sales.

2. Background

- 2.1. This chapter sets out the regulatory framework including some of the key duties and obligations on the Authority and gas transporters (GTs) that need to be considered when developing a proposed licensing regime to support a divested industry structure in the event that DN sales proceed. The description of the regulatory framework includes an outline of the current licence framework including relevant sections of the Gas Act 1986 (the Gas Act).
- 2.2. This chapter also explains the process to date including both the September document and the consultation through the Development and Implementation Steering Group (DISG).
- 2.3. This chapter therefore outlines:
- ◆ the regulatory background; and
 - ◆ the progress to date.

Regulatory background

The onshore regulatory framework

- 2.4. This section sets out some of the key elements of the regulatory framework that are relevant in the context of the proposed DN sale as follows:
- ◆ The Gas Act; and
 - ◆ Transco's GT licences

The Gas Act

- 2.5. The Gas Act provides for the regulation of the onshore gas regime in Great Britain and for the separate licensing of GTs, gas shippers and gas suppliers. This section sets out some of the key relevant areas of the Gas Act for consideration.

Duties of the Authority

- 2.6. Section 4AA of the Gas Act provides that the principal objective of the Authority in carrying out its functions under the Gas Act is to protect the interests of consumers in relation to gas conveyed through pipes, wherever appropriate, by promoting effective competition between those engaged in, or in commercial activities connected with, the shipping, transportation or supply of gas. Consumers for these purposes includes both existing and future consumers.
- 2.7. In carrying out its functions under the Gas Act in a manner which is best calculated to further the principal objective, the Authority is required to have regard to the following:
- ◆ the need to secure that, so far as it is economical to meet them, all reasonable demands in Great Britain for gas conveyed through pipes are met; and
 - ◆ the need to secure that licence holders are able to finance the carrying on of the activities which they are authorised or required to do.
- 2.8. In performing its duties, the Authority must have regard (amongst other consumers) to the interests of individuals who are disabled or chronically sick, of pensionable age, with low incomes or residing in rural areas.
- 2.9. The Authority may, in carrying out any of its functions, have regard to the interests of consumers in relation to electricity, telecommunications, and water and sewerage services, which are affected by the carrying out of those functions.
- 2.10. The Authority must carry out its functions in the manner it considers is best calculated to:
- ◆ promote efficiency and economy on the part of authorised persons and the efficient use of gas conveyed through pipes;
 - ◆ protect the public from dangers arising from the conveyance of gas through pipes or the use of such gas;
 - ◆ to contribute to the achievement of sustainable development; and
 - ◆ secure a diverse and viable long term energy supply.

- 2.11. The Authority must also have regard to the effect on the environment of activities connected with the conveyance of gas through pipes.
- 2.12. In carrying out its functions in accordance with the above objectives and duties, the Authority must have regard to:
- ◆ the principles under which regulatory activities should be transparent, accountable, proportionate, consistent and targeted only at cases in which action is needed; and
 - ◆ any other principles appearing to the Authority to represent the best regulatory practice.
- 2.13. In addition, the Authority must, in carrying out its functions, have regard to any guidance issued by the Secretary of State about the making by the Authority of a contribution towards the attainment of any social or environmental policies set out or referred to in the guidance.

Duties of Gas Transporters

- 2.14. In addition to meeting the Authority's statutory duties, the licence framework post DN sales must permit the NTS and DNs to fulfil their own statutory obligations under the Gas Act as GTs. These include the duty of each GT to:
- ◆ develop and maintain an efficient and economical pipeline system (section 9(1)(a) of the Gas Act);
 - ◆ facilitate competition in the supply of gas (section 9(1A) of the Gas Act); and
 - ◆ avoid any undue preference or undue discrimination in the terms on which it undertakes to convey gas (section 9(2)(b) of the Gas Act).

The licensing framework

- 2.15. Sections 5 to 8A of the Gas Act provide for the licensing of activities relating to gas. These include the licensing of GTs, gas shippers and gas suppliers. Unlike the Electricity Act 1989, the Gas Act does not provide for the separate licensing of transmission and distribution activities. Section 7 of the Gas Act sets out the

provisions relating to the licensing of GTs. Section 8 provides for standard conditions of licences.

2.16. Section 23 of the Gas Act sets out the provisions relating to the modification of licence conditions for which there are a number of different procedures. These are set out below:

- ◆ **Collective licence modification (CLM).** The CLM procedure deals with the modification of standard conditions under Section 23(1)(b) and Section 23(7) of the Gas Act. The Authority may bring forward proposals for licence modification and the CLM arrangements enable relevant licence holders who are not content with a proposed modification to a standard condition to register their formal objection. Numerical tests determine the level of objections to a proposal which is measured against a blocking minority threshold prescribed by the Secretary of State. In the absence of the blocking threshold being met, the Authority may direct that a proposed modification be made; and/or
- ◆ **Individual consent.** The individual consent process as set out in sections 23(1)(a) and 23(6) of the Gas Act requires the Authority to gain the consent of each relevant licensee prior to modification of the licence. This process can be used either in relation to amending standard conditions for individual licensees or amendments to special conditions for individual licensees. Where a standard condition has been modified by individual consent, it ceases to be subject to the CLM procedure to the extent that it has been modified.

2.17. In the absence of obtaining consent either through the CLM procedure or the individual consent of the relevant licensee, the Authority may refer the matter to the Competition Commission for resolution. The Gas Act provides the mechanism by which licences can be modified in the circumstances of such a reference.

2.18. Under Section 8AA of the Gas Act a licence is capable of being transferred by the licence holder with the consent of the Authority, in accordance with the section, and any terms of the licence relating to its transfer. This may include conditions which must be complied with before the licence can be transferred.

Consent may be given subject to compliance with such modification or other conditions as the Authority considers necessary.

Transco's GT licences

2.19. At the time of publication of the September document, Transco plc had one operative GT licence. Now, Transco plc is the holder of six largely identical GT licences⁸. Transco's original GT licence covers the operation of its high pressure transportation business, largely the National Transmission System (NTS), and its lower pressure distribution business (mainly the DNs). It also applies to LNG Storage arrangements and metering. Looking at the conditions in Transco's original GT licence and the five new additional GT licences, it is clear that some conditions relate to its:

- ◆ NTS operations;
- ◆ DNs operations; and
- ◆ both NTS and DN operations.

2.20. The original GT licence and the five new additional GT licences currently have no distinction between conditions relating to the NTS and DNs. Accordingly, it is clear that Transco's original GT licence and the five new additional GT licences cover many aspects of its business on an integrated basis reflecting the fact that the NTS and DNs have been operated within a single legal entity and under one licence (i.e. the original GT licence).

2.21. Transco's original GT licence and the five new additional GT licences have three types of conditions⁹. These are as follows:

- ◆ **Standard Conditions.** These are applicable to all holders of GT licences including IGTs¹⁰, unless otherwise modified or specified. These

⁸ Following consideration of respondents' views, in November 2004, Ofgem granted five new GT licences to Transco plc. These new additional GT licences largely mirror the original Transco plc licence that was operative prior to this date. As at the date of this consultation document all gas transportation assets owned by Transco were operated pursuant to its original GT licence. As at the date of this consultation document the five new additional GT licences whilst active do not relate to any particular gas transportation assets owned or operated by Transco. This issue is discussed in more detail later in this Chapter.

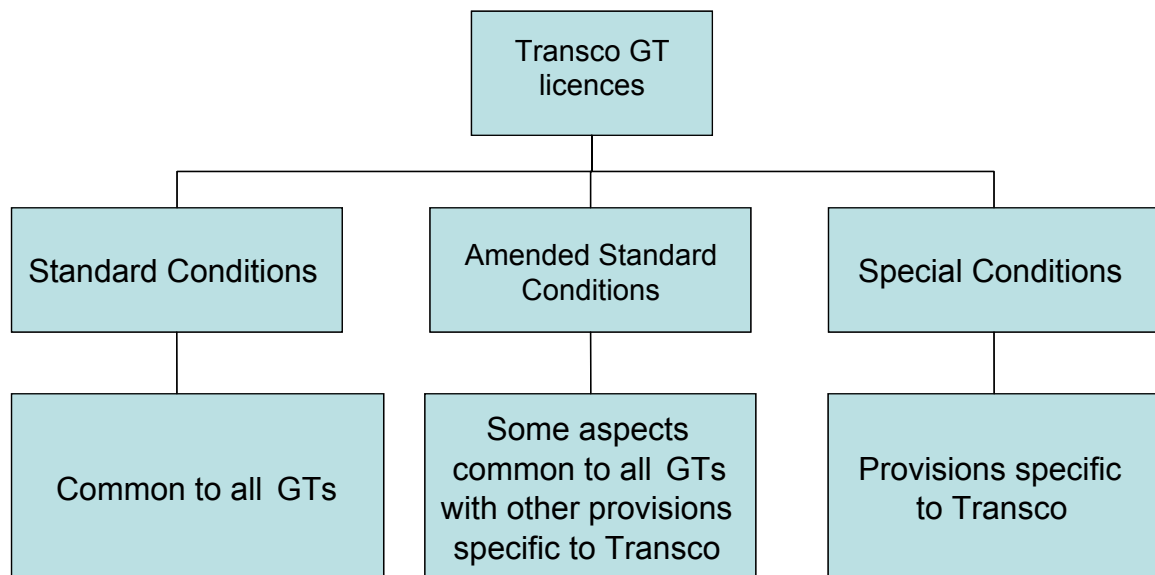
⁹ The Gas Act 1986 refers only to conditions or Standard Conditions – the terms Amended Standard Conditions and Special Conditions have been developed to differentiate between the types of conditions and the processes of modification applicable to them.

conditions were designated by the Secretary of State in September 2001 and have been updated by Ofgem since that time through the CLM procedure;

- ◆ **Amended Standard Conditions.** These are conditions where the wording of the standard condition has been amended with the consent of the relevant licensee (i.e. pursuant to sections 23(1)(a) and 23(6) of the Gas Act) to reflect a particular need or characteristic of the licensee. The amendments are not subject to the CLM procedure; and
- ◆ **Special Conditions.** These are specific to individual licensees and have been introduced with the relevant licensee's consent (i.e. pursuant to sections 23(1)(a) and 23(6) of the Gas Act) in order to reflect a particular need or characteristic of the licensee.

2.22. Figure 2.1 below illustrates the current structure of Transco's original GT licence and the five new additional GT licences.

Figure 2.1: Configuration of Transco plc's existing GT licences



¹⁰ IGTs are existing independent gas transporters which are not currently owned by Transco plc. These IGTs, in general, operate small scale networks which serve groups of domestic customers and are therefore much smaller than any of the transmission or distribution networks owned by Transco plc. References to distribution networks (DNs) or Independent Distribution Networks (IDNs) within this document refer to the DNs currently owned and operated by Transco plc and those proposed for sale by Transco plc respectively.

2.23. All standard conditions in Transco's original GT licence and the five new additional GT licences are currently split into 3 sections, as follows:

- ◆ Section A of the standard conditions contains conditions relating to interpretation, application and payments;
- ◆ Section B of the standard conditions contains general provisions; and
- ◆ Section C of the standard conditions contains transport services obligations.

2.24. Conditions contained in Section C of the standard conditions are currently the only ones in the GT licence capable of being switched on or switched off (i.e. for the provisions to be active or not active over a particular period) by a direction of the Authority issued with the relevant licence holder's consent (pursuant to Standard Condition 2).

Process to date

2.25. This section sets out an overview of the process that Ofgem has followed to date in relation to licensing issues. In particular it sets out an overview of:

- ◆ the consultation relating to the granting of additional GT licences to Transco;
- ◆ the September informal licence consultation document;
- ◆ the granting of five new additional GT licences to Transco; and
- ◆ the involvement of the industry workgroups.

Grant of licence consultation

2.26. In the context of its proposed DN sale, in July 2004 Transco applied to Ofgem for eight new additional gas transporter (GT) licences relating to the restricted geographical area associated with each of its DNs. The applications were submitted prior to the announcement by Ofgem that NGT would not have to legally separate each of the DNs it is proposing to retain (the RDNs) and, as

such, eight new additional licences were requested in order to accommodate this possibility.

- 2.27. Following Transco's application, in July 2004 Ofgem issued a notice under the Gas Act in relation to the potential grant of new additional GT licences to Transco to accommodate the proposed DN sale and invited views from interested parties regarding this proposal. This consultation was open for a period of two months.

September informal licence consultation document

- 2.28. In September 2004 Ofgem issued an informal consultation document regarding the proposed restructuring of Transco's original GT licence and the five new additional GT licences¹¹. This document invited the views from interested parties in relation to the possible modifications to Transco's original GT licence and the five new additional GT licences (if granted) in the context of the proposed sale of one or more DNs by Transco. Ofgem considered that modifications, in relation to both the content and structure of these licences, would be required in the context of a potential DN sale to ensure that the scope of the regulatory framework was sufficient to support a divested industry structure, so that customers' interests were protected.
- 2.29. In the September licence consultation Ofgem detailed that it would review the need to modify Transco's existing GT licence and the five new additional GT licences as part of the DN sales process through:
- ◆ the November 2004 Section 23 notice (appended to this document as Appendix 5);
 - ◆ the Section 8AA consent to the transfer of Transco's GT licences to wholly owned subsidiaries (in relation to GT licences which are proposed to be transferred from Transco to wholly owned Transco subsidiary companies) in February 2005 (and associated additional

¹¹ *National Grid Transco – Potential sale of gas distribution network business, Initial Thoughts on restructuring of Transco plc's Gas Transporter Licences, Consultation document, Ofgem, September 2004, 215/04*

Section 23 notice in relation to GT licences which will be retained by Transco);

- ◆ as part of the conditions attached to the Authority's consent to dispose of the relevant DN assets under the Amended Standard Condition 29 (Disposal of Assets); and
- ◆ a second Section 23 consultation prior to completion of the proposed transaction (if required). This may be necessary in order to accommodate any further licence amendments that may be required to reflect the development of arrangements to support a post-DN sales environment.

2.30. In the September document, Ofgem conducted an initial analysis of each of the standard and special conditions in Transco's original GT licence, to assess the extent of amendments that would be required to incorporate the implementation of arrangements in the event that a DN sale takes place. In this regard Ofgem undertook an evaluation of the licence conditions in Transco's original GT licence that, in a divested industry structure, would be appropriate to transmission activities (which would apply to the NTS), distribution activities (which would apply to the RDNs and the independent DNs (IDNs)) and both transmission and distribution activities (which would apply to the NTS, RDNs and IDNs).

2.31. Ofgem also considered whether new licence conditions would need to be introduced into Transco's original GT licence and the five new additional GT licences to reflect a divested network structure and consulted upon the possible provisions that could be implemented to accommodate metering and LNG Storage arrangements going forward.

2.32. This preliminary analysis concluded that a significant number of modifications would be required to Transco's original GT licence and the five new additional GT licences to address the regulatory issues associated with a potential DN sale.

This is a direct consequence of the currently integrated nature¹² of Transco's business which is reflected in its current GT licence.

- 2.33. Appendix 3 sets out Ofgem's proposed treatment of each licence condition as set out in the September consultation document.

Grant of licence decision

- 2.34. Following consideration of responses received in relation to the notice issued, on 5 November 2004 the Authority (without in any way fettering its discretion in relation to the proposed transaction) granted five new additional GT licences to Transco.¹³ The five new additional licences were approved on the basis that they can be revoked in the event that the proposed disposal of DN assets from Transco to wholly owned Transco subsidiaries does not proceed. The grant of five GT licences reflects the Authority's decision not to insist on legal separation between each of Transco's RDNs and, as such, these entities will be retained under one DN-GT licence. It also accommodates Transco's commercial decision to sell four of its DNs. Transco has formally withdrawn its remaining three applications.
- 2.35. The five new additional DN-GT licences were granted and remain in substantially the same form as Transco's existing GT licence. As at the date of this document, all gas transportation assets owned by Transco were operated pursuant to its original GT licence. As at the date of this document, the five new additional GT licences, whilst active, do not relate to any particular gas transportation assets owned or operated by Transco. Once the modifications proposed in the attached Section 23 notice are made, each of the five new additional GT licences will relate to specific DN assets and Transco's original GT licence will relate to the NTS assets only.

¹² As explained above, Transco's original GT licence covers a number of different activities including: transmission; distribution; LNG storage; and metering.

¹³ Notice under section 7B(9)(c) of the Gas Act 1986 of the grant of five new additional gas transporter licences. This document is available on the Gas Distribution Network Sale page of Ofgem's website.

Legal separation

2.36. The conclusions document on offtake arrangements¹⁴ outlined the Authority's position that it was minded to require Transco to undertake legal separation and targeted structural separation. As described in the Final Impact Assessment¹⁵, Ofgem has been working closely with NGT in recent months to understand the implementation issues that would need to be addressed should legal separation be pursued. In the course of this investigation, it became apparent that pursuing full legal separation of the NTS and the RDNs would be likely to prove problematic. This is because:

- ◆ moving NGT's NTS business into a new legal entity would create two low probability risks that could, were either to materialise, create significant costs to customers. These risks are that:
 - ◆ third party contracts that reference Transco's Network Code might need to be adjusted; and
 - ◆ the wholesale gas market might fragment into a number of individual Network Codes with separate market arrangements in each.
- ◆ moving NGT's RDN business into a new legal entity is likely to create disproportionate costs for NGT associated with debt restructuring.

2.37. The Authority therefore concluded that it would not be appropriate to require legal separation of the RDNs and the NTS as part of the DN sales process.

2.38. Ofgem considers that Transco plc will require two licences under the proposed new arrangements; one for the NTS and one for the RDNs. The remainder of this document has been drafted on this basis.

¹⁴ National Grid Transco, Potential sale of network distribution businesses, Offtake Arrangements Conclusions document on framework, August 2004

¹⁵ National Grid Transco, Potential sale of network distribution businesses, Final Impact Assessment, November 2004, pp. 72 – 74.

Involvement of industry workgroups

- 2.39. In recent months, the focus of discussions in the DISG has turned towards the licensing regime. Indeed, licensing issues have been on the agenda at each DISG meeting since the release of the September document.
- 2.40. In particular, DISG 19 (held on 14 September) was devoted to a review of Transco plc's original GT licence and five new additional GT licences and Ofgem's proposed changes to support DN sales with a view to protecting the interests of customers. This session helped interested parties to familiarise themselves with the broad range of licensing issues. In addition, Ofgem was able to obtain preliminary feedback in relation to the proposed treatment of each of Transco's existing licence conditions.¹⁶ Minutes of this meeting are provided in Appendix 4.
- 2.41. More recently, DISG members have provided comments on Transco's initial drafting of specific proposed licence conditions. In the period since 19 October (DISG 22), the group has discussed a variety of key licence conditions, including initial drafting relating to:
- ◆ NTS and DN price controls;
 - ◆ the condition that establishes a requirement to prepare a Network Code (i.e. ASC 9, in Transco's original GT licence);
 - ◆ conditions relating to the charging of gas shippers (i.e. ASC 4 & 4A, in Transco's original GT licence);
 - ◆ procurement and use of system management services (NTS & DN);
 - ◆ permitted and prohibited procurement activities;
 - ◆ LNG (for both NTS and DNs);
 - ◆ the establishment of a requirement not to prejudice the operation of other networks;

¹⁶ DISG 19 was attended by, amongst others, representatives of NGT, potential purchasers, shippers, IGTs and the HSE.

- ◆ DN incentive scheme and performance reporting;
- ◆ long term development statements; and
- ◆ first line emergency response service to the operator of the NTS.

2.42. DISG members have provided feedback both at the DISG meetings and in written format after the meetings. This process has been an important contribution to Ofgem's consultation on the proposed restructuring of Transco plc's original licence and new additional GT licences.

2.43. It should be noted that, whilst some of the detailed comments provided by DISG members are reflected in the appropriate sections of this document, this is not intended to exhaustively reflect all comments which were received. Some issues have instead been logged on the DISG issues list, and will be progressed further within that forum.

3. Section 23 notice and formal consultation

- 3.1. As outlined in Chapter 1, Ofgem is consulting in this document on formal changes to the Transco original GT licence and the five new additional GT licences, proposed through the attached Section 23 notice.
- 3.2. Ofgem is also separately consulting informally on the modifications expected to be included through the 8AA process (with an accompanying additional Section 23 notice for Transco's retained businesses/GT licences).
- 3.3. The purpose of this chapter is to set out the changes that are proposed through the Section 23 notice attached in Appendix 5.
- 3.4. This chapter sets out:
- ◆ the process;
 - ◆ respondents' views on the proposed Section 23 modifications that were published in September;
 - ◆ Ofgem's proposals for changes at the Section 23 stage; and
 - ◆ details of the modifications proposed under the Section 23 process.

Process to date

- 3.5. Following the release of the September consultation document, in September 2004, Ofgem also published in outline the expected modifications that it would be proposing at the Section 23 stage. Broadly, the proposed modifications were designed to have two effects:
- ◆ to separate the price controls into individual licences so that the original Transco GT licence only contains the NTS price control and four of the new additional GT licences contain the price controls for the DNs (with one new additional GT licence containing the 4 RDN price controls); and
 - ◆ to restructure the licence consistent with the September licence consultation having regard to respondents views.

- 3.6. In October 2004, these potential changes were discussed at the DISG. The views of DISG members have been included in the next section which sets out respondents' views to the September consultation document.

Respondents' views

- 3.7. Ofgem received nine responses to the informal Section 23 drafting which was included in the September document. Of these, three potential purchasers provided comments and five shipper/suppliers gave their views, as well as NGT, representing Transco. The views expressed by DISG members have also been included in this section for completeness.

Price control conditions

- 3.8. Five responses were submitted in relation to the proposed amendments to the price control conditions of the NTS and DNs. These responses were received from one potential purchaser, three shipper/suppliers and NGT. Overall, the responses were supportive of Ofgem's proposals although the potential purchaser requested clarification regarding certain areas of the drafting. The points raised are outlined in turn in the following section.
- 3.9. Two shipper/suppliers and NGT expressed support for Ofgem's proposal not to reopen Transco's existing price control, although in contrast, one shipper/supplier was of the opinion that it would be necessary for Ofgem to reconsider its position on this. This shipper/supplier perceived that, as arrangements to be implemented in a post-DN sales environment reach resolution, detailed analysis and drafting would be required to accommodate these. As a general point, a potential purchaser also set out that any new revenue flows and incentive mechanisms introduced as part of the offtake and interruptions reforms should be reflected. In NGT's response, it considered that any requirement for detailed specification of offtake arrangements could be accommodated by an Exit Capacity Release Methodology Statement.
- 3.10. One potential purchaser perceived that, in relation to the treatment of shrinkage within the price control, further clarification would be required, while in contrast, NGT was of the opinion that it would not be appropriate for the shrinkage provisions to be amended as a result of a DN sale.

- 3.11. In addition, the same potential purchaser indicated that it would require an improved understanding of the way in which the delay to the DN sales process, as a result of the Gas Act exemptions issue, would impact upon the price control conditions, particularly in relation to the financial year in which changes would be made. This potential purchaser additionally had some more specific concerns regarding the drafting of the price control licence conditions proposed within the September document. As an overall concern, they considered that it would be important for Ofgem to ensure that the price control provisions were adequately reflected within each of the DN-GT licences.
- 3.12. The same potential purchaser also highlighted that it was unsure how the term “prescribed rates” would operate within the DN special condition regarding the Restriction of Revenue in respect of the Distribution Network Transportation Activity. In particular, they had concerns that if separate rating assessments were not undertaken where a company were to own more than one DN, the ratings would need to be split within the DNs and that, as drafted, provisions for ratings to be split are only made if NGT were to continue to hold all of the DNs and the NTS. In addition, this potential purchaser was unsure as to how prescribed rates would be allocated to each of the IDNs.
- 3.13. The same potential purchaser expressed concern regarding amendments to price control conditions for reasons unrelated to DN sales. This potential purchaser particularly mentioned the apparent deletion, within the NTS licence of the SOK term, and that DN related provisions in relation to the exit capacity investment incentive revenue had been deleted. Detailed drafting points were also made in relation to the DN specific price control condition, noting that in paragraph 8 (1)(i) and 8 (4)(i) the reference to 1 April 2004 should be a reference to 1 April 2005.

Restructuring of the licences

- 3.14. Seven responses were received regarding the restructuring of Transco’s original GT licence and the new additional GT licences following a potential DN sale. Of these, three were submitted on behalf of potential purchasers and a further four were submitted on behalf of shippers/suppliers. A range of views were expressed in this regard although, in general, respondents had concerns with respect to the structure of the licences proposed and requested further

clarification regarding the way in which the arrangements would work in practice. The views expressed are set out in turn below.

- 3.15. Two potential buyers expressed support for the proposed structure of the licences and the introduction of a new standard special condition which would overcome the problem of modifying amended standard conditions. One of these potential buyers considered that it would be appropriate for the NTS and the DNs to have licence-specific special conditions, introduced or modified only with the consent of the licensee. However, both respondents had concerns regarding the way in which the structure of the licences, in which these new standard special conditions were to be incorporated, had been developed.
- 3.16. In particular, these two potential purchasers expressed support for the incorporation of NTS and DN specific conditions into separate sections that relate explicitly to the NTS and DN but had concerns that standard special conditions should not be developed which would be applicable to both the NTS and the DNs. One of these potential purchasers considered that following a potential DN sale, it may be necessary to implement amendments within the licence of one class of entity and not the other and that this could prove complicated if the condition were applicable within the NTS and DN section of the licence. Similarly, the other potential buyer that responded on this was of the opinion that licensees should only be subject to conditions regarding the activity that they are responsible for undertaking and that, as such, it should not be possible for either the DNs or the NTS to influence the licence conditions of the other.
- 3.17. Four shipper/suppliers and another potential buyer also expressed concerns regarding the proposed structure of the licences. In particular, although this potential buyer and two of these shipper/suppliers acknowledged that the changes to the structure would be necessary to accommodate a divested industry structure, they considered that the proposed licence structure was unnecessarily complex and, in this respect, confusing. Two of the shipper/suppliers were of the opinion that any additional complexity could contribute further cost and difficulty into the modification process. In a similar regard, another shipper/supplier had concerns that a multiplicity of different types of licence condition should not be introduced as this may make the licence structure confusing. The potential purchaser also suggested that it would be beneficial for

Ofgem to establish and develop separate transmission and distribution licences to reflect the new industry structure.

- 3.18. A further shipper/supplier considered that issues in relation to the restructuring of the licences were not as complex as Ofgem had envisaged. As such, this shipper/supplier suggested that it would be possible to use the “switch on/switch off” conditions to accommodate any differences between IGTs and DN-GTs and, in this respect, retain a single set of proposed changes at the Section 23 stage.

Ofgem’s proposals for changes at the Section 23 stage

- 3.19. Having carefully considered respondents’ views, Ofgem has decided to limit the scope of the proposed modifications, to the Transco original GT licence and the five new additional GT licences, in this Section 23 notice to modifications aimed at separating the price controls rather than attempting to restructure the licences at this stage. Chapters 4 and 5 of this document discuss respondents’ views on the licence restructuring and Ofgem’s proposed way forward on these issues as part of the Section 8AA process.
- 3.20. Ofgem is therefore proposing to modify the following special conditions in each of Transco’s licences as part of the Section 23 notice provided in Appendix 5:
- ◆ Special Condition 28A (Revenue restriction definitions);
 - ◆ Special Condition 28B (Restriction of revenue in respect of the NTS transportation owner activity, Distribution Network transportation activity and NTS system operation activity);
 - ◆ Special Condition 29 (Allocation of revenue and costs for the calculations under the price control);
 - ◆ Special Condition 30 (Supplementary provisions for revenue restrictions);
 - ◆ Special Condition 33 (Information to be provided to the Authority in conjunction with the transportation system revenue restriction);
 - ◆ Special Condition 34 (Licensee’s methodology for determining incremental entry capacity volumes);

- ◆ Special Condition 35 (NTS performance reporting);
- ◆ Special Condition 36 (LDZ incentive scheme and performance reporting); and
- ◆ Schedule A (NTS output measures for the price control).

3.21. The original GT licence will be modified so that it contains the price control for the NTS only. One of the new additional GT licences will be modified to contain the price controls for the following DNs that are planned to be retained by Transco:

- ◆ North West;
- ◆ East of England;
- ◆ West Midlands; and
- ◆ London.

3.22. Each of the remaining four new additional GT licences held by Transco, will be modified to contain the price controls for the following DNs of which NGT is planning to dispose:

- ◆ Scotland (potential purchaser:- consortium comprising Scottish & Southern Energy plc, Borealis Infrastructure Management Inc and Ontario Teachers Pension Plan (hereafter referred to as SSE));
- ◆ North of England (potential purchaser:- consortium including Cheung Kong Infrastructure Holdings Ltd/United Utilities plc);
- ◆ Wales and the West (potential purchaser:- a consortia led by Macquarie European Infrastructure Fund); and
- ◆ South of England (potential purchaser:- SSE).

3.23. As at the date of this document, all gas transportation assets owned by Transco were operated pursuant to the original GT licence. As at the date of this document, the five new additional GT licences, whilst active, do not relate to any particular gas transportation assets owned or operated by Transco. Once the

modifications proposed in the attached Section 23 notice are made, each of the five new additional GT licences will relate to specific DN assets (as set out above) and Transco's original GT licence will relate to the NTS assets only.

- 3.24. As discussed in Chapter 2, whilst Ofgem has decided not to require the legal separation of Transco's NTS and its RDN businesses, Ofgem proposes, for clarity of structural separation requirements between these two entities, that Transco will, following DN sales, be the holder of two GT licences – one for its NTS business, and one for its RDN businesses. This decision is reflected in the modifications outlined above.
- 3.25. These modifications also reflect the decision taken by SSE that the two DNs for which it is a potential purchaser, should be in separate legal entities and separately licensed.
- 3.26. For the avoidance of doubt, Ofgem will not direct the modifications contained within the Section 23 notice until after the Authority has considered, in the middle of January 2005, whether to grant its consent to the proposed sales. In issuing this notice, it is important to make clear that there can be no expectation on the part of NGT, Transco, potential DN purchasers, shippers, suppliers or any other interested parties either as to the Authority's final decision in relation to the proposed transaction or as to the regulatory framework which may eventually be implemented if the Authority consents to the proposed transaction.
- 3.27. The information in this notice is not binding on the Authority. Nothing in this notice is to be construed as granting any rights or imposing any obligations on the Authority. The Authority's discretion will not be fettered by any statements made in this notice.
- 3.28. As part of the proposed transaction, Transco is proposing to hive-down four of its DN businesses to four wholly owned Transco subsidiary companies. The proposed hive-down by Transco will require, inter alia, the consent of the Secretary of State and the Authority pursuant to Amended Standard Condition 29 of the original Transco licence. It is expected that both the Secretary of State and the Authority will decide on this matter in mid January 2005. The modifications to the original Transco GT licence and the five new additional GT licences which are set out in this Section 23 notice (contained in Appendix 5) would not be directed by the Authority in the event that Transco does not obtain the

consents necessary to undertake the hive-down of the DNs from Transco to the wholly owned Transco subsidiary companies.

Details of the proposed modifications

- 3.29. In this section, we consider the detail of the proposed modifications for each of the special conditions, in the Transco Original GT licence and the five new additional GT licences that Ofgem proposes to change as part of the Section 23 notice in turn. This commentary highlights the key changes proposed, but it should be noted that housekeeping corrections and cross-referencing amendments will also be made as appropriate and are included in the proposed drafting within the Section 23 notice provided in Appendix 5.

Special Condition 28A: Revenue restrictions definitions

Description

- 3.30. This condition defines a number of terms in the revenue restrictions.

Proposed changes

- 3.31. This special condition will need to be amended and split into separate special conditions setting out the definitions that are relevant for each DN licence and the NTS licence.
- 3.32. Appendix 8 contains a table setting out, for each definition, whether it is common to NTS and DN-GTs, or is applicable only to the NTS or DN-GTs.
- 3.33. In summary, and without limitation, the following changes are also proposed to be made to the NTS licence with respect to this special condition:
- ◆ in each case, the title of the condition is proposed to be amended to make it clear that the condition applies to the NTS transmission owner activity and system operation activities;
 - ◆ cross-references to other special conditions, whose titles are proposed to be changed are proposed to be amended as appropriate;

- ◆ references to “LDZs” are proposed to be changed to “Distribution Network” as appropriate;
- ◆ “Distribution Network” is proposed to be redefined by inserting the mapping of LDZs to DNs previously included within paragraph 6A of Part 1b; and
- ◆ “Supply of LDZ services” is proposed to be modified such that it is titled “supply of Distribution Network services” and the services which are **not** covered are proposed to be more clearly defined.

3.34. In summary, and without limitation, the following changes are also proposed to be made to the DN-GT licences with respect to this special condition:

- ◆ the title of the condition is proposed to be amended to make it clear that it applies to the Distribution Network;
- ◆ cross-references to other special conditions, whose titles are proposed to be changed are proposed to be amended as appropriate;
- ◆ references to “LDZs” are proposed to be changed to “Distribution Network” as appropriate, unless the references are required to maintain consistency with the current version of the Network Code;
- ◆ “Distribution Network” is proposed to be redefined by inserting the mapping of the relevant LDZs to DNs previously included within paragraph 6A of Part 1b in relation to the DN concerned;
- ◆ where appropriate, references to the licensee’s Network Code are proposed to be changed to reference Transco plc’s Network Code;
- ◆ the formula year for DNs is proposed to be redefined such that $t = 1$ commences on 1 April 2004 rather than 1 April 2002, to allow the full separation of the price control provisions contained within Special Condition 28B;
- ◆ references to “NTS firm exit capacity” and other related terms are proposed to be retained such that the definition of “NTS transportation owner” which is required in Special Condition 28B within the section on

“prescribed rates” is complete, and that all terms referred to within this definition (and the definition of those terms in turn) are provided; and

- ◆ “Supply of LDZ services” is proposed to be modified such that it is titled “supply of Distribution Network services” and the services which are **not** covered are more clearly defined.

Special Condition 28B – Restriction of revenue in respect of the NTS transportation owner activity, distribution network transportation activity and NTS system operation activity

Description

3.35. This special condition defines the price controls and incentives applicable to the NTS and DNs (other than those for LNG and metering activity which are subject to separate price controls). The condition is split into three parts:

- ◆ Part 1 a: The NTS transportation owner activity revenue restriction;
- ◆ Part 1 b: The LDZ transportation activity revenue restriction; and
- ◆ Part 2: The NTS system operation activity revenue restriction.

Proposed changes

3.36. This special condition will need to be amended and split into separate special conditions setting out the revenue restriction relevant for each licensee and each DN where appropriate.

3.37. For the Transco plc licence containing provisions relating to the NTS, in summary and without limitation, the following modifications are proposed:

- ◆ the title of the special condition is proposed to be amended to make it clear that it is applicable only to NTS assets and not DNs;
- ◆ Part 1a has a number of modifications proposed. These are:

- ◆ with respect to the term TOF_t , changes are proposed to clarify the requirements with respect to “NTS prescribed rates” while all of the DNs are retained within Transco plc; and
- ◆ the formula deriving TOK_t for 1 April 2002 (and associated provisions), will be removed and replaced with the calculated value¹⁷.
- ◆ Part 1 b is proposed to be deleted as this sets out the LDZ transportation activity restriction which is no longer required in the NTS licence; and
- ◆ Part 2 of the condition is proposed to be modified to:
 - ◆ redefine the term I_t (as the definition was incorrect in the current licence as it referred to TOK_t , not SOK_t);
 - ◆ remove any references to LDZs from the exit incentive; and
 - ◆ amend cross-references to other price control related conditions where their title has changed.

3.38. For each of the Transco plc licences containing provisions relating to the DNs, in summary and without limitation, the following modifications are proposed:

- ◆ the title of the special condition is proposed to be amended to make it clear that this is a special condition applicable to DNs;
- ◆ sub-headings are also proposed to be provided as appropriate indicating the DNs to which the DN revenue restriction provisions apply. For the avoidance of doubt it is proposed that within the licence for the RDNs each revenue restriction is separate for each network that Transco plc proposes to retain;
- ◆ Part 1a of the existing condition is proposed to be deleted as this applies to the NTS TO activity revenue restriction;

¹⁷ The rationale for these amendments is that as the TOK_t term for 2002 is now known with certainty, the terms deleted are now superfluous, and therefore a single term has been inserted in order to simplify this condition.

- ◆ Part 1b of the condition is proposed to be modified as follows:
 - ◆ the title is proposed to be changed so that a previous reference to “LDZ” is now to “Distribution Network”;
 - ◆ Section 6A of the licence which defines DNs with reference to their constituent local distribution zones (LDZs) is proposed to be deleted;
 - ◆ with respect to the term DNF_t , changes are proposed to clarify the requirements with respect to “Distribution Network prescribed rates” while all of the DNs are retained within Transco plc;
 - ◆ throughout the condition where tables set out the values for all DNs, these are proposed to be removed and replaced with the relevant values for that DN only;
 - ◆ the “i” subscripts within the relevant price control parameters are proposed to be removed to reflect the specificity of the provisions to each DN, and references such as “in respect of the relevant Distribution Network” is proposed to be removed as they will no longer be required following separation of this condition;
 - ◆ in order to allow the relevant revenue restrictions to be allocated to individual DNs, the price control formula year for $t = 1$ will be specified as commencing on 1 April 2004 i.e. the date on which the gas distribution price controls were separated. As such, where appropriate, regulatory formulae will be re-based to 2004. For example, with respect to the derivation of the DNZ_t term, the number specified for 2002 and the formula for 2003 will be deleted and a derived number for 2003 (i.e. DNZ_{t-1} for formula year commencing 1 April 2004) will be inserted. However, it should be emphasised that this will not change the outcome of the price control for any of the DNs; and
 - ◆ redefine the term I_t (the definition of which was previously within Part 1a which will be deleted).

- ◆ Part 2 of the condition will be deleted as this applies to NTS SO activity revenue restriction, except for the "statement of actual interruption".
- ◆ this includes the deletion of DN related revenue provisions. For the DNs, these provisions relate to the exit capacity investment incentive revenue incentive for greater than 15 days of interruption. Ofgem has considered whether such provisions should be introduced into the licences of the DNs. However, following the recent application of a cap and collar to this incentive across the NTS and DN incentives of +/- £1 million, Ofgem has reached the conclusion that the amount of money that relates to the DNs as a whole is very small. The combined outturn target level for this incentive for formula year 2003/4 was £61.30million. The LDZ greater than 15-day interruption part was £1.47 million, representing 2% of the total target. Applying this percentage to the +/- £1 million cap/collar would lead to a cap/collar of +/- £20,000, and therefore the equivalent amount on an individual DN is even smaller; however
- ◆ Ofgem has taken the decision that only the provisions that relate to the "statement of actual interruption" should remain at this time; furthermore
- ◆ Ofgem would note that the nature of exit regimes enforced will need to be considered as part of the Section 8AA process.

3.39. It is noted that Ofgem is conducting a parallel consultation with respect to the proposed changes to Special Condition 28B of Transco plc's original GT licence and the five new additional GT licences. This consultation relates to the income adjusting event provisions within this special condition, and will affect the drafting relating to the determination of any adjustment factor to be applied to the SORA_t term within paragraph 14(11) of Special Condition 28B of the GT licences.

3.40. Respondents should also note that Ofgem has issued today a separate unrelated but parallel Section 23 notice relating to proposed modifications to the Income Adjusting Events provisions of Transco's GT Licences. This proposes changes

with respect to Special Condition 28B of Transco's Licences and will affect the drafting relating to the determination of any adjustment factor to be applied to the SORAt term within paragraph 14(1) of Special Condition 28B of the Transco Licences (the "SORAt modification")

- 3.41. Without fettering the Authority's discretion, it is likely that the SORAt modification, if made, would be directed on 00:00 hours on 27 January 2005. The modifications proposed by this Notice are likely to be made after this date. As such, if the SORAt modification is made, the modifications proposed in this notice would be based upon Special Condition 28B as modified by the SORAt modification.
- 3.42. It should be noted that these are parallel consultations and are not interdependent. This modification and the modifications proposed in this notice are capable of being made without the SORAt modification.

Special Condition 29 - Allocation of revenue and costs for the calculations under the price control

Description

- 3.43. This special condition sets out the licensee's obligations regarding the allocation or attribution of revenues, costs, assets and liabilities by the licensee in order to calculate the values referred to in Special Condition 28B.

Proposed changes

- 3.44. This special condition needs to be amended and split into special conditions setting out the provisions that are relevant for each DN-GT licence and the NTS-GT licence. As such, in summary and without limitation, it is proposed that modifications will be made such that:
- ◆ the title clearly indicates whether the condition relates to the NTS or Distribution Networks;
 - ◆ cross-references to other special conditions, whose titles are changing are proposed to be amended as appropriate;

- ◆ the activities specified within paragraph 2, that do not apply to the NTS or DNs are proposed to be deleted from the NTS and DN licences respectively; and
- ◆ the activities specified within paragraph 8, under the definition of “transportation business”, which no longer apply, are proposed to be excluded.

Special Condition 30 – Supplementary provisions of the revenue restrictions

Description

- 3.45. This special condition sets out activities that can be treated as excluded services and defines the charges or proportions of the charges which can be treated as excluded services. These include last resort payments, supplementary charges, emergency service charges, charges relating to gas illegally taken or works at connection points. Other services outside of normal activity or for the specific benefit of third parties can also be treated as excluded services, if approved by the Authority. The Authority can direct that previously excluded services should no longer be treated as such.

Proposed changes

- 3.46. This special condition needs to be amended and split into special conditions setting out the provisions that are relevant for each DN-GT licence and the NTS-GT licence. As such, in summary and without limitation, it is proposed that modifications are made such that:
- ◆ the title clearly indicates whether the condition relates to the NTS or Distribution Networks;
 - ◆ cross-references to other special conditions, whose titles are changing are proposed to be amended as appropriate;
 - ◆ paragraph 2 is proposed to be amended such that only the parts of Special Condition 28B that remain applicable to the licensee are covered; and

- ◆ paragraph 4 is proposed to be amended such that only the activities that remain applicable to the licensee remain in sub-paragraph (b).

Special Condition 33 - Information to be provided to the Authority in conjunction with the transportation system revenue restriction

Description

- 3.47. This special condition requires the licensee to provide statements to the Authority incorporating the information that it set out in specified tables. In each case, this table specifies the piece of information, the period over which it should be provided, the frequency of provision and the reporting deadline for its provision. Where information is derived from the application of a licence formula, the component parameters in the formula should be reported. All revenue information provided must comply with the requirements of Special Condition 29 (Allocation of revenue and costs for calculations under the price control).

Proposed changes

- 3.48. This condition is proposed to be split appropriately for the NTS and DN-GTs. This special condition is designed to also ensure that information is provided for each network, including each of Transco's RDNs.
- 3.49. As such, in summary and without limitation, changes are proposed to be made such that:
- ◆ the title clearly indicates whether the condition relates to the NTS or Distribution Networks;
 - ◆ cross-references to other special conditions whose titles are changing are proposed to be amended as appropriate; and
 - ◆ only the tables (and associated definitions within these) which remain relevant to the licensee are proposed to be included.

Special Condition 34 – Licensee’s methodology for determining incremental entry capacity volumes

Description

- 3.50. This special condition requires licensees to prepare and submit each year an audited incremental entry capacity release methodology statement setting out the methodology by which it will determine whether to make incremental entry capacity available for sale to the shippers.

Proposed changes

- 3.51. This special condition is only applicable to the NTS. As such, this condition is unused within the licences of DNs, and is inserted into the NTS-GT licence unchanged (except for cross-referencing adjustments).

Special Condition 35 – NTS performance reporting

Description

- 3.52. This special condition provides for the collection of information by the licensee to an appropriate degree of accuracy, to monitor the environmental performance of the NTS and facilitate the development of an expenditure monitoring framework.

Proposed changes

- 3.53. This special condition is only applicable to the NTS. As such, this condition is unused within the licences of DNs, and is inserted into the NTS-GT licence unchanged (except for cross-referencing adjustments).

Special Condition 36 – LDZ incentive scheme and performance reporting

Description

- 3.54. This special condition defines the incentive and performance measures applicable to Transco’s DNs.

Proposed changes

3.55. This special condition is only applicable to the DN licences. As such, this condition is unused within the NTS licence, and is proposed to be inserted in to the DN-GT licences largely unchanged with modifications only to:

- ◆ include “Distribution Network” rather than “LDZ” in the title and within the licence drafting as appropriate. As such, the definition of “LDZ network” will be removed, and “Distribution Network” will be redefined with reference to Special Condition 28A; and
- ◆ reflect necessary cross-referencing adjustments.

Schedule A – NTS output measures for the price control

Description

3.56. Schedule A to Transco plc’s original GT licence and five new additional GT licences provides baseline output measures pursuant to Part 1a and Part 2 of Special Condition 28B, for:

- ◆ NTS TO baseline entry capacity;
- ◆ Initial NTS SO baseline entry capacity;
- ◆ NTS baseline firm exit capacity; and
- ◆ NTS baseline interruptible exit capacity.

Proposed changes

3.57. This Schedule is only applicable to the NTS. As such, this schedule is unused within the licences of DNs, and will be inserted into the NTS-GT licence unchanged (except for cross-referencing adjustments).

Views invited

3.58. The proposed drafting for each of these conditions is provided within the Section 23 notice within Appendix 5. In this Appendix, the proposed changes relative to

the versions of Transco plc's original GT licence and five new additional GT licences which are currently in force are highlighted in revision marking.

- 3.59. In order to make the modifications set out in the notice to the original Transco GT licence and each of the five new additional Transco GT licences Transco's consent will be required in accordance with the requirements of Section 23(6) of the Gas Act as it will be the holder of the relevant licences at the relevant time. This means that only Transco will be asked to provide consent to the proposed modifications. This consent, if provided by Transco, would enable the Authority, but not oblige it, to direct that the modifications be made.
- 3.60. However, in light of the proposed transaction, Ofgem would particularly hope to receive comments on the proposed modifications to the original Transco GT licence and the five new additional GT licences from, amongst others, potential DN purchasers and other interested parties.

4. Key issues

4.1. In the September document a number of key issues regarding proposed changes to the licensing regime in the event the sale of the DNs proceeds were raised. Following consideration of respondents' views, and the extensive discussion of issues of concern with interested parties at meetings of the DISG, Ofgem has revised this list of key issues and reconsidered its position with respect to these issues.

4.2. In this chapter we:

- ◆ describe each of the issues within this revised list of key issues;
- ◆ provide a summary of respondents' views on these issues; and
- ◆ set out Ofgem's proposals with respect to each issue, in the light of respondents' comments to date.

4.3. The key issues considered within this chapter are structured as follows:

- ◆ structure of licences, including new conditions proposed in relation to the private collective licence modification (CLM) and switch on / switch off provisions;
- ◆ governance, including provisions relating to transportation charging and the Network Code / Uniform Network Code (UNC);
- ◆ system security, including provisions relating to emergency services coordination and pipeline security standards;
- ◆ clarification of shipper / GT obligations in the light of proposed offtake arrangements;
- ◆ price controls and incentive arrangements;
- ◆ system operator managed service arrangements (SOMSAs);
- ◆ standards of performance (including connections);
- ◆ business separation; and

- ◆ treatment of LNG and metering.

Structure of licences

4.4. In this section, we consider key issues that relate to the structure of the licences proposed in the event of DN sales. The key issues fall under two main headings:

- ◆ the private CLM procedure; and
- ◆ the switch on / switch off provisions.

4.5. These are considered in turn below.

Private CLM procedure

The September document

- 4.6. In the September document, Ofgem proposed a 'private' CLM procedure. Ofgem additionally set out its proposals for restructuring the special conditions of Transco's GT licences. Ofgem explained that its preliminary analysis had concluded that a significant number of modifications would be required to Transco's existing licences to address the regulatory issues associated with any DN Sale.
- 4.7. The most significant impact of these (potentially extensive) modifications would be that many of the current standard conditions would become amended standard conditions. This would mean that the statutory CLM procedure, would cease to apply to the standard conditions to the extent that they were modified. Given the potential scale of the modifications, Ofgem considered that this would, in practice, make the statutory CLM procedure largely unavailable.
- 4.8. The statutory CLM procedure provides the Authority with the ability to modify standard conditions across classes of licences without the consent of every holder of such licence. Ofgem considered that to lose the ability to consistently modify licences in a divested industry structure would not be in the interest of customers nor consistent with best regulatory practice.

Respondents' views

- 4.9. In total eight respondents commented on this issue. Three of these respondents expressed their support for the underlying principle behind the introduction of the private CLM procedure, although their support was subject to the resolution of certain outstanding issues in this regard. Two potential purchasers, had concerns regarding the equitability of GT treatment under the proposed modification procedure which is discussed further in Chapter 6. A shipper/supplier also expressed support but considered that it would be more appropriate to introduce the private CLM procedure it as a standard condition within the GT licences in order to make it applicable to all transporters, including IGTs. This shipper/supplier was of the opinion that this would be especially important in view of the fact that implementation of the private CLM was intended to ensure consistency between the licences of all GTs.
- 4.10. While a potential purchaser acknowledged that Ofgem's approach to the development of the private CLM procedure is supported by the provisions of the Gas Act, two shipper/suppliers questioned the legal robustness of this proposed licence condition. One shipper/supplier expressed doubts that the Authority could modify gas transporters licences without recourse to statutory procedures¹⁸ and suggested alternative approaches that may address the issues raised. These alternative approaches included the application of a switch on / switch off approach to address the differences between IGTs and DN-GTs or the use of the Secretary of State's power under Section 41C of the Gas Act to decompose the activity of gas transportation into two separately licensable activities of gas transmission and gas distribution.
- 4.11. Although one shipper/supplier understood the rationale underlying the proposed private CLM procedure it also questioned whether this would require a statutory process. As such, it suggested that it might be better to accept the inflexibility associated with the individual consent until a new revised statutory procedure could be introduced rather than introducing a potentially confusing private CLM process at this stage.

¹⁸ This respondent considered that section 7(B)(7)(b) of the Gas Act does not allow such modifications except where either the modification, or its detailed policy objective, is itself spelt out in the conditions in advance.

- 4.12. Energywatch expressed concern that the proposed approach was overly complex and may undermine the standard conditions within the licence. However, energywatch also noted that losing the ability to consistently modify GT licences would not be in the interests of customers.
- 4.13. In a similar regard, two potential purchasers considered that the provisions that could be used by GTs under the private CLM procedures would not be dissimilar to those available to Ofgem through the requirement to gain individual consent to a licence modification. In particular, they considered that the procedures under the private CLM would effectively permit each DN-GT to exercise the power of veto in relation to any proposed amendment and would not therefore provide Ofgem with any additional authority to pursue licence modifications.
- 4.14. Respondents' views regarding the voting rules and thresholds applied to collective voting are discussed in Chapter 6, where the proposed drafting of this new licence condition is discussed in detail.

Ofgem's proposals

- 4.15. Ofgem continues to consider it appropriate to restructure the NTS and DN GTs licences and to introduce the private CLM procedure. Overall, Ofgem continues to believe that the licence structure it proposed (and associated private CLM procedure) will safeguard the interests of present and future customers. Furthermore, we consider that this structure is robust to any future changes in industry structure, for example, if NGT were to dispose of any further networks.
- 4.16. Ofgem also conducted further analysis of Transco plc's existing licences. In addition to its analysis that it set out in the September document that a number of standard conditions would potentially require modification as a consequence of NGT's potential disposal of assets, Ofgem notes that a large number of Transco's licence conditions are Amended Standard Conditions. With the notable exception of the provisions of LNG, the majority of other amendments to the designated standard conditions would need to apply to NTS and DN – GTs. Given that it is proposed that these licences will not be under common ownership, Ofgem considers it is important to protect the interests of customers

to have a mechanism to ensure that collective licence modification remains a possibility under any divested industry structure.

- 4.17. Ofgem notes two respondents' concerns with regard to the potential legality of the private CLM procedure, but having analysed the points raised by respondents', continues to believe that the introduction of the private CLM as proposed in the September document is appropriate. It should be noted that Ofgem developed its proposals within the limitations of the current statutory framework. Its analysis of this framework determined that it was not possible to define a new licensable activity, as the activity of gas transportation covers both transmission and distribution. It is for these reasons that Ofgem has adopted this 'private' CLM procedure.
- 4.18. With regards to the alternative solutions proposed by one respondent, Ofgem notes that:
- ◆ with respect to the use of switch on / switch off provisions to address IGT / DN GT differences, the Gas Act plainly allows standard conditions in an individual GT licence to be modified by agreement with the licence holder and without any potential veto rights vesting in IGTs, who can make representations under Section 23(3); and
 - ◆ under Section 41C of the Gas Act, the Secretary of State cannot make licensable what is already licensable. Therefore, as explained above, as the activities of gas transmission and gas distribution are already licensable, the Secretary of State does not have powers to split the activity of gas transportation into two separately licensable activities of gas transmission and gas distribution.
- 4.19. Ofgem considers it important to note that a private CLM procedure can only be introduced into the licence with the consent of the relevant licensee as it would necessarily need to be introduced as a special licence condition. As a result, Ofgem would not be able to introduce private CLM procedures into other licences without licensee consent.
- 4.20. Furthermore, although, in relation to GT licences, the Gas Act contains no equivalent of section 8(7) and Section 23(6) (which concern modifications to standard conditions in gas supplier and gas shipper licences only), it is Ofgem's

intention to seek to ensure that any modifications under the private CLM procedure do not unduly disadvantage IGTs.

- 4.21. With regards to other issues of structure, Ofgem remains of the opinion that those conditions that apply to both NTS and DN-GTs should, in general, be described as such within the licence, and treated accordingly.
- 4.22. The private CLM licence conditions proposed are discussed in further detail in Chapter 6.

Switch on/switch off

The September document

- 4.23. In the September document, Ofgem considered that it would (where possible) seek to revert the amended standard conditions (and certain special conditions) in Transco's existing GT licence and, if granted, the new additional GT Licences, to the standard conditions designated by the Secretary of State, as updated by Ofgem pursuant to the statutory CLM procedure. However, this may not be appropriate in every case and, where a modification is required to a standard condition, Ofgem proposed to repeat the relevant standard condition as a standard special condition which could be subject to the private CLM procedure. Therefore Transco and the owners of the DNs would be subject to two similar conditions in respect of the same issue. Ofgem therefore proposed, as part of the process for modifying Transco's GT licences, to "switch off" those standard conditions that have been replaced by standard special conditions.
- 4.24. Ofgem proposed, pursuant to section 7(B)(7)(a) of the Gas Act, to introduce a new special condition enabling the Authority to also switch on or switch off standard conditions in sections A and B¹⁹, with the consent of the licence holder. As with Standard Condition 2, this switch would be capable of being used in relation to entire conditions or parts of conditions and would not be time limited, enabling it to be used in the future²⁰.

¹⁹Section C of the Standard Conditions of the GT licence is already capable of being switched on or switched off under Standard Condition 2.

²⁰ In the September 2004 informal licence consultation document, Ofgem considered that it was satisfied that the introduction of this switch and the use of it in the context of DN sales would not cause any undue

Respondents' views

- 4.25. Out of the three respondents to this issue two expressed their support for the introduction of the proposed switch condition.
- 4.26. One potential purchaser noted that the switch condition was a necessary adjunct to the proposals to create standard special conditions. However, this potential purchaser considered that it would be helpful if this condition could contain the criteria under which it would be applicable. The potential purchaser considered that its use should be restricted to technical problems related to the creation of the relevant conditions.
- 4.27. Another potential purchaser stated that it would seem appropriate that the switch on / off mechanism would be common to all the NTS and DN owners and be introduced as a standard special condition into part A of both the NTS's and DNs' Special Conditions. However, the potential purchaser stated that it is vital that the new condition provides for the consent of the licensee to any individual licence condition being switched on / off.
- 4.28. Finally, one respondent questioned the legal basis of this proposal under section 7(B)(7)(a) of the Gas Act.

Ofgem's proposals

- 4.29. In Ofgem's view there is a clear legal basis for the switch on / switch off provisions proposed. As noted by one respondent the need for such a condition is intrinsically linked to the private CLM proposals discussed above.
- 4.30. As stated in the September document, the main circumstance that will lead to the requirement for the Authority to be able to switch off standard conditions will be when it is necessary to modify an existing standard condition, and therefore create a new standard special condition and switch off the original standard condition. However, the switch on / switch off provisions cannot have an explicit linkage between the switch on of standard special conditions and switch off of standard conditions as, in certain circumstances, it may be

discrimination against IGTs (who would not have such a switch in their licences).

necessary to switch off all or part of a standard condition without there being an explicit replacement.

- 4.31. In Ofgem's view, this condition should be a standard special condition based upon the existing Standard Condition 2, which will require the explicit consent of the licensee to the switching on or off of a particular standard condition. It is not appropriate for this to be a standard special condition solely applicable to NTS and DN-GTs as it may be the case that a standard condition remains relevant to NTS GTs but not DN-GTs. As such, this is proposed as a standard special condition applicable to NTS and DN-GTs combined, as well as a standard special condition for the NTS and a standard special condition for DNs.
- 4.32. The new switch on / switch off licence conditions proposed are discussed in further detail in Chapter 6.

Governance

- 4.33. In this section, we consider key issues that relate to the governance of regulatory and commercial arrangements in the event of any DN sales. The key issues fall under two main headings:

- ◆ transportation charging arrangements; and
- ◆ the Network Code / UNC.

- 4.34. These are considered in turn below.

Transportation charging arrangements

The September document

- 4.35. Ofgem, in response to concerns raised within the workgroups, considered that:
- ◆ the Joint Office (JO) should have responsibility for administering the coordination of modifications to the distribution charging arrangements, ensuring that the development of charging methodologies is coordinated across the industry. The document noted that this would not preclude the development of different charging methodologies should the Authority consider this to be appropriate; and

- ◆ GTs should be obliged to use reasonable endeavours to announce changes to charges on one specific date each year.

Respondents' views

- 4.36. Overall, of the thirteen respondents who commented on this issue the majority were supportive of Ofgem's proposals. Eight of the respondents commenting on this issue expressed their support for the proposed coordination role for the Joint Office.
- 4.37. Five shipper/suppliers were concerned that the proposals did not specifically prohibit divergence in charging methodologies, and that the emergence of different charging methodologies may increase users' costs.
- 4.38. Furthermore, energywatch expressed concern that such an obligation could create a peak workload for shipper/suppliers that could affect the rigour with which proposals are assessed.
- 4.39. Respondents were broadly supportive of proposals to introduce a reasonable endeavours obligation on NTS and DN-GTs to announce changes to charges on one specific date each year. This approach was particularly favoured by shippers who expressed concern regarding the imposition of costs on users should there be a lack of co-ordination with respect to charges.
- 4.40. One potential purchaser proposed that there should be a specific date for changes to transportation charges each year, and stated a preference for 1 April, in order to synchronise changes to charges with the start of the accounting (and price control) year, whilst another respondent preferred 1 October to coincide with the start of the "gas year".
- 4.41. However, some concerns were also expressed regarding the reasonable endeavours obligation:
 - ◆ NGT noted that under the current arrangements there will be at least four changes a year to NTS charges. NGT therefore, suggested that the NTS licensee should be excluded from the licence conditions relating to the frequency of changes to transportation charges;

- ◆ concerns were also expressed regarding the interaction of the reasonable endeavours obligation and the revenue recovery obligation:
 - ◆ two shipper/suppliers were concerned that, even under a reasonable endeavours obligation, charges may still change more than once a year, especially given the interaction with the obligation on GTs not to exceed their allowed revenue;
 - ◆ NGT stated that should changes to charges only be made on certain specified dates in the year, then greater under/over recovery should be allowed through modification of the appropriate licence conditions; and
 - ◆ a potential purchaser agreed that the proposed obligation on GTs should be a reasonable endeavours obligation and noted that this would be “subordinate” to the best endeavours obligation not to exceed allowed revenue.

4.42. Comments were also received through DISG on this issue. Three shipper/suppliers supported the reasonable endeavours obligation and stated that the certainty of once a year changes was important. One shipper/supplier stated that the reasonable endeavours obligation and changes to charges only once a year, in October, will achieve charge stability during contract periods.

4.43. In subsequent discussions NGT has stated that it would be willing to commit to a reasonable endeavours obligation to change administered charges only twice a year (on 1 April and 1 October). This proposed frequency is in line with the TO commodity charge and the 150 day notice period. However, NGT has argued that if this obligation is implemented, then the consequent risk of under / over charging will increase. NGT has therefore argued that the under / over recovery provisions are modified such that dead-bands are introduced so that a penal interest rate is not applied to each £1 of overspend. Such a modification would bring provisions into line with the National Grid Company (NGC) electricity licence, which currently applies a 2% dead-band to revenue over-recovery such that only the standard base rate applies within this band. NGT has stated that, in its view, a 2% dead-band would be applicable to the DNs, with a 5% dead-band applicable to the NTS.

Ofgem's proposals

- 4.44. Ofgem agrees with the majority of respondents that changes to the governance arrangements for transportation charges are necessary as part of any DN sale.
- 4.45. However, Ofgem considers that the frequency of charge changes needs to be revisited in light of the decision to adopt an Option 2A approach to offtake arrangements. Under the Option 2A approach, DNs would act as an intermediary for payment flows, and therefore there would be no payment flows directly from shippers to the NTS. As a result, a DN would be required to pass through changes to NTS charges to shippers using its network through its own charges. This means that, if the NTS changes its charges on more than an annual basis, this would have implications for the frequency with which a DN would need to change its charges. Ofgem therefore does not believe that it would be appropriate for the obligation upon the NTS-GT to differ to that placed upon DN-GTs.
- 4.46. Ofgem has considered NGT's response, and proposes to revise its proposals so that a reasonable endeavours obligation to change all charges only twice a year on 1 April and 1 October is introduced. This is reflected within the drafting of Standard Special Condition A4 Charging Gas Shippers – General, within Appendix 7B, and discussed within the appropriate section of Chapter 5.
- 4.47. Ofgem recognises that NGT may receive requests for entry capacity pricing information at new entry points within any charging year. Such requests may require additional changes to entry capacity charges, over and above Transco's reasonable endeavours obligation, and will be reviewed by Ofgem on a case by case basis.
- 4.48. Ofgem has noted NGT's proposals for a dead-band within which a standard interest rate would apply, and acknowledges that such a provision would bring the condition into line with NGC's electricity licence. Such a provision has not been introduced into the licence drafting provided in Appendix 7B; however, Ofgem would welcome views from respondents as to whether such a provision should be included, and if so, the appropriate size of such a dead-band for both the NTS and the DNs.

- 4.49. In respect of the specific points raised by respondents, Ofgem recognises that its proposals do not preclude divergences between charging methodologies where Ofgem considers this to be appropriate. Ofgem recognises that in certain situations it might be appropriate to allow divergence in charging methodologies to enable DN owners to be innovative in the operation of their networks. Ofgem is aware that there may be costs to shippers associated with such divergences in charging methodologies and will take this into consideration when considering whether to use its right to veto changes to methodologies.
- 4.50. In relation to the point raised by a respondent that the reasonable endeavours obligation does not preclude *per se* a DN-GT licensee from changing its charges more frequently, Ofgem again considers that a total restriction would not be appropriate. However, to fulfil the reasonable endeavours obligation Ofgem would expect DN owners to provide clear and compelling arguments as to why additional changes were required in the light of unforeseen changes to circumstances.

Network Code and offtake arrangements

The September document

- 4.51. Ofgem invited views on the proposed establishment of a Uniform Network Code (UNC), with its modification process managed by the Joint Office. In particular, Ofgem invited views on whether the commercial aspects of the offtake arrangements should be:
- ◆ integrated into the UNC (the UNC only approach); or
 - ◆ separate to the provisions of the UNC with a single set of overarching governance arrangements that apply to both agreements, which was NGT's preferred approach at that time.
- 4.52. Following extensive discussions at workgroups, Ofgem's initial view was that the current Network Code should be replaced by the UNC and Short Form Network Codes (SFCs) specific to each NTS and DN-GT but that reference the UNC²¹.

²¹ It has still to be determined whether Transco plc shall be requested to have one or two SFCs.

- 4.53. Furthermore, as a result of the conclusions in the Agency RIA and of discussions in workgroups, Ofgem's view was that the modification process for the UNC should be managed by the Joint Office (with Amended Standard Condition 9 of Transco's licence being amended accordingly).

Respondents' views

- 4.54. There were differing views on the appropriate structure of the UNC. In total ten respondents commented on this issue.

- 4.55. Five respondents expressed their support for the UNC only approach. Points raised by these respondents included the following:

- ◆ one shipper/supplier stated that a separate offtake code could introduce cross governance issues similar to those that occur in electricity industry (because of the stand-alone nature of major industry codes);
- ◆ one shipper/supplier supported the offtake code should come under the governance of the UNC as this will maintain the integrity of the existing end to end Network Code arrangements;
- ◆ one shipper/supplier stated that the arrangements should minimise costs and avoid unnecessary complexity; and
- ◆ one shipper/supplier stated that the UNC only approach would be the option most likely to maintain the integrity of the existing network arrangements.

- 4.56. Five respondents supported the UNC plus offtake code approach. The following comments were made by these respondents:

- ◆ one potential purchaser stated that a UNC plus offtake code approach would be most appropriate, as the alternative would allow unaffected parties to amend the arrangements; and
- ◆ NGT stated that following a UNC only approach could undermine clarity and accountability of the roles and responsibilities of GTs and shippers.

- 4.57. However, in a letter to Ofgem in October 2004, NGT noted that its preference for the UNC plus offtake code approach was based on an assumption of how the

offtake arrangements would operate. Given changes in these assumptions, NGT noted that the logic and approach of trying to keep the arrangements separate was no longer appropriate, and that commercial arrangements should sit within the UNC.

Ofgem's proposals

- 4.58. Following consideration of respondents' views, Ofgem is minded to adopt a UNC only approach, with the modification process for the UNC managed by the Joint Office. The technical operator to operator arrangements would be contained in separate bilateral agreements, so that unaffected parties could not raise any modifications to these documents.
- 4.59. The following affected licence conditions are discussed in further detail later in this document:
- ◆ Chapter 5: Standard Special Condition A11 Network Code (formerly Amended Standard Condition 9); and
 - ◆ Chapter 6: Standard Special Condition A12 Joint Office Governance Arrangements.

System security

- 4.60. In this section, we consider key issues that relate to system security in the event of DN sales. The key issues fall under two main headings:
- ◆ emergency services coordination; and
 - ◆ pipeline security standards.
- 4.61. These are considered in turn below.

Emergency services coordination

September document

- 4.62. In the September document, in response to concerns raised through the work group process, Ofgem outlined a number of issues relating to the coordination of emergency services. These were:

- ◆ responsibility for incidents occurring at DN boundaries;
- ◆ first response emergency services to IGTs; and
- ◆ first response emergency services to NTS.

DN boundaries

4.63. It is essential that, where incidents occur close to network boundaries (or in instances where it is not immediately possible to identify on which network the emergency has occurred), it is clear which DN has responsibility to provide “make safe” emergency services. In the September document, Ofgem proposed placing a licence condition on DNs obliging whichever DN is notified of such incidents to despatch an engineer and provide “make safe” emergency services regardless of the network on which it transpires that the incident has actually occurred. Ofgem also invited views on the treatment of liabilities associated with the potential obligation to make safe an incident, regardless of the ownership of the network.

First response emergency services to IGTs

4.64. In the September document, Ofgem invited views on whether to place a licence condition upon the DN-GTs, obliging them to make first response emergency services available to IGTs at a “reasonable rate”. Ofgem also invited views on whether those services should be limited only to those services considered to be monopoly emergency services, or to include those that might be considered to be available on a commercial basis (such as ongoing repair and restoration services).

First response emergency services to NTS

4.65. Currently, Transco responds to incidents on the NTS using the DN field force in which the incident occurs. Transco have suggested in workgroup discussions that it would not be efficient for the NTS to provide its own emergency response field force given the infrequency of incidents on the NTS and the need to respond to any incident within one hour. In the September document, Ofgem welcomed respondents’ views on whether, as suggested by Transco, it would be

appropriate for the DN-GTs to be obligated under the terms of their licences to provide first response emergency services to the NTS-GT at a reasonable rate.

Respondents' views

DN boundaries

- 4.66. In total eighteen respondents commented on this issue with fifteen specifically stating that they supported the introduction of a licence condition governing emergency response to incidents at DN boundaries. Two respondents, one IGT and one shipper/supplier, highlighted the need to ensure that the present arrangements continue. NGT stated that the boundary arrangements are already covered by the DN safety cases, and there is no need to duplicate these arrangements. One shipper/supplier stated that it had mixed views on this issue since risk and liability issues could arise as a result of DN GT engineers working on third party networks. A potential buyer stated that the incidence of "incorrect" calls should be monitored.
- 4.67. The Gas Industry Safety Group suggested that differentiation should be made between gas emergencies arising within premises and those on the network itself. This respondent suggested that, while a licence condition relating to emergencies within premises should be put in place, the position with regards to emergencies on the network itself is more complex as engineering personnel could be put at risk if any more than an initial assessment is obligatory under the terms of a licence condition.
- 4.68. Energywatch stated that the coordination of emergency services and the restoration of supply will be a critical success factor for the new regime and that any significant differences in the arrangements for handling emergencies would jeopardise safety and customer service.
- 4.69. One potential buyer raised quality concerns, stating that services provided under a licence condition should be to the same standard as if the DN was working on its own network. This respondent also stated that liability for physical damage caused by negligence should be included in the condition, while economic and consequential loss should be excluded. This respondent also stated that it would expect an indemnity against third party claims, and would not expect a DN to have to employ additional staff or equipment to meet this condition.

- 4.70. One respondent was supportive of an NGT proposal that information relating to an overlapping 5km boundary “strip” should be made available on adjoining networks to facilitate the provision of emergency services.

First response emergency services to IGTs

- 4.71. Eighteen respondents responded to this issue. One potential purchaser agreed to this condition in its current form and one shipper/supplier stated the proposal seemed reasonable. Another potential purchaser agreed to the condition in its current form but stated that it would prefer it to include 1st line emergency response.
- 4.72. Six respondents, four shipper/suppliers, one IGT and one potential purchaser stated that the condition should be extended to monopoly emergency services.
- 4.73. Three shipper/suppliers, one IGT, one respondent and GISG stated that the condition should include all emergency services and repair and restoration services.
- 4.74. Energywatch stated that the same arrangements should apply to emergencies whether they arise on a GT’s own network, on another DN, on an independent GT’s network or on Transco’s NTS.
- 4.75. One respondent stated that ‘major loss of supply’ needs to be defined to ensure that all DNs have comfort in what a ‘major loss of supply’ is.
- 4.76. NGT stated that there should be a condition requiring first line emergency responses for each DN. NGT stated that DNs should continue to provide IGT services under existing commercial contracts.

First response emergency services to NTS

- 4.77. Thirteen respondents specifically supported NGT’s proposal that DNs should be obliged to provide first line emergency response to the NTS. One potential purchaser suggested that the proposed approach could be undertaken as an interim solution until the next price control.
- 4.78. Another potential purchaser opposed this proposal and stated that this is a service that Transco can provide and, if it chooses not to, can be subject to a

commercial arrangement. One shipper/supplier believed the obligation should be in line with the obligation to provide this service to the IGTs and be subject to the same reasonable market rate that it charges to IGTs thus ensuring that accurate costs are reflected.

- 4.79. Energywatch stated that the same arrangements should apply to emergencies whether they arise on a GT's own network, on another DN, on an independent GT's network or on Transco's NTS.

Ofgem's proposals

DN boundaries

- 4.80. Ofgem continues to believe it is important for arrangements to be in place between DNs regarding the provision of emergency services at DN boundaries. Ofgem understands from NGT that these will form a part of the GTs' safety cases, and therefore arrangements will have to be in place to the satisfaction of the Health and Safety Executive (HSE). For this reason, Ofgem considers that it would be inappropriate to impose a licence obligation relating to this.

First response emergency services to IGTs

- 4.81. Ofgem has given careful consideration to all of the responses it has received on this issue. Ofgem has also considered carefully, consistent with its duties, the aspects of emergency service provision that arise as a consequence of the potential fragmentation of Transco's transportation business.
- 4.82. Ofgem notes that the majority of responses considered that additional licence conditions (either with respect to "make safe" and / or "repair and restoration") are necessary as part of DN sales. Ofgem, however, considers that the key difference between the status quo and any divested structure would be the number of network owners that an IGT may have to interface with will increase (by, on NGT's current plans, three). Ofgem recognised that this may give rise to additional costs in its impact assessment, and welcomes views on this issue.
- 4.83. Under the status quo, IGTs have a commercial contract for the provision of these services, which currently encompass both "make safe" and "repair and restoration". The concern that respondents expressed concerning negotiating with a monopoly business for these services is not therefore a consequence of

any disposal by NGT of DN assets given this concern exists under the current industry framework as well. For this reason, Ofgem does not consider it appropriate to introduce new licence conditions at this stage. However, Ofgem would invite views to this informal consultation on this point.

- 4.84. Ofgem notes that since the September document, NGT has extended the duration of its current commercial contract by six months. Prior to the expiration of the current contract, Ofgem will undertake a review of the provision of these services. This review will, as requested by some parties, include a full assessment of the extent to which repair and restoration services are contestable activities. Following this review Ofgem will propose any GT licence modifications it considers necessary to protect the interests of customers.

First response emergency services to NTS

- 4.85. Ofgem considers that the DNs should be obliged by licence condition to provide emergency services to make safe any emergency on the NTS at a reasonable rate. This is discussed further in Chapter 6, under “Inter-operator service agreements.” Drafting of this condition is also provided in Appendix 7B (Standard Special Condition D6 Provision of First Call Emergency Response to the Operator of the NTS).
- 4.86. Ofgem considers that the DNs should be obliged by licence condition to provide to make safe on the NTS. The costs for the provision of this service are and should continue to be recovered through the price controls of the DNs. This approach is appropriate because of the very low number of calls to incidents on the NTS, the inefficiency of each DN having to write contracts, bill and recover costs from the NTS and the fact that this service does not have nor will ever possibly have any element of contestability. This approach differs from the approach taken in respect of the provision of first response emergency services by the DNs to the IGTs.
- 4.87. Ofgem considers it is appropriate to address this issue within the scope of DN sales as the issue arises as a direct consequence of fragmentation of ownership between the NTS and DNs.

Pipeline security standards

September document

- 4.88. In the September document, Ofgem explained that there is an obligation on Transco to develop the network to meet daily demand for gas, such that the ability of the pipeline system to meet that demand is only expected to be exceeded in 1 year out of 20 based on the previous 50 years of data (i.e. the “1 in 20 obligation”).

Respondents’ views

- 4.89. A number of respondents commented specifically on this issue, the majority of these stating that they considered it appropriate for current security standards to apply to all NTS and DN-GT licences. One shipper/supplier also added that they considered that the methodology by which compliance with this obligation is measured should be explicitly defined and included with the UNC (in order to provide increased transparency to network users).
- 4.90. One potential purchaser supported the inclusion of the 1 in 20 obligation in all NTS and DN-GT licences, but noted that the ability for DNs to comply with this requirement would be dependent upon securing an appropriate allocation of exit capacity from the NTS.
- 4.91. In contrast, one shipper/supplier stated that it was not clear that the NTS should be subject to the 1 in 20 obligation, on the basis that (under Option 2 of the offtake arrangements) it will be obliged to deliver NTS exit capacity consistent with requests from NTS direct connects.
- 4.92. Through comments received at DISG meetings one shipper/supplier stated that it was important that this condition was considered as part of the offtake arrangements.

Ofgem’s proposals

- 4.93. Ofgem agrees with the majority of respondents that the 1 in 20 obligation should at this time apply to all GTs including NTS and DN-GTs. As such, Standard

Condition 16 (Pipeline System Security Standards) will continue to apply to all NTS and DN-GTs as discussed in Chapter 5 later in this document.

- 4.94. However, Ofgem has identified that Standard Condition 16 may require modification of a technical nature to reflect NGT's diurnal storage proposals. At present, customers directly connected to the NTS are required to purchase a level of maximum daily offtake quantity (MDQ) that is consistent with their maximum hourly offtake quantity (MHQ), and each customer is not permitted to exceed 1/24th of its MDQ in any given hour. Under the offtake arrangements, it is proposed that NTS offtake flexibility will be defined as a separate product that is allocated and traded in the same way as firm NTS exit capacity. This will enable some customers to meet their required level of MHQ through the purchase of NTS offtake flexibility, and reduce their purchased level of MDQ accordingly.
- 4.95. This may have technical implications given that Transco's "1 in 20" obligation (as currently worded) requires it to design the system to meet "peak aggregate daily demand". As such, it may be necessary to modify Standard Condition 16 to reflect Transco's proposals for the flexibility product. These modifications would be to make the obligation a standard special condition applicable to all NTS and DN-GTs to deliver the level of MHQ requested by NTS connectees as well as MDQ.
- 4.96. In any such modification, Ofgem would seek to ensure that the revised condition has the same effect as it currently has under Transco's common ownership. As these issues are still in consideration in Transco's exit development forum, as part of this document Ofgem will not be proposing any modifications or providing any drafting relating to Standard Condition 16. It is therefore proposed at this stage that Standard Condition 16 will apply to all GTs including NTS and DN licensees. However, if Ofgem considers later in the process that such modifications are required these will be informally consulted upon through the DISG.
- 4.97. Ofgem would welcome views from respondents on how this issue should be addressed.

Clarification of shipper / GT obligations

4.98. In the event of DN sales, it will be necessary for offtake arrangements to be put in place between the NTS and the DNs for the offtake of gas from the NTS²².

The DTI is currently consulting upon whether an exemption under the Gas Act should be granted to allow such arrangements (which are defined as shipper activities under the Gas Act) to be made²³.

4.99. In the event that an exemption is granted, and the proposed offtake arrangements (i.e. an Option 2A approach) are confirmed, it will be necessary to make a number of small changes to the provisions of each of Transco's licences seeking to ensure that:

- ◆ the NTS / DN interface implied by implementation of an Option 2A approach is fully reflected; and
- ◆ to ensure that there is clarity regarding shipper and GT obligations.

4.100. In order to ensure that an Option 2A approach is fully reflected within the licence, the following will need to be considered:

- ◆ the adaptation of the price control conditions to reflect the fact that DNs will be passing through NTS charges to shippers (the allowed DN revenues will need to increase to reflect this cost pass-through);
- ◆ inclusion of incentive regimes in relation to the NTS / DN interface as discussed below; and
- ◆ reflecting the fact that GTs will be charging other GTs in the charging related licence conditions, and ensuring that any obligations that relate to the provision of information to (or by) shippers should apply to GTs where appropriate, given proposed arrangements.

²² Absent implementation of a shipper led approach for booking exit capacity, which was consulted upon in the Offtake RIA, and met with strong opposition from industry participants.

²³ *Proposed exemption for certain gas transporters from a prohibition on conducting particular shipper activities – Consultation on statutory instrument.* Department for Trade and Industry, November 2004.

4.101. These requirements are not included in the licence drafting in Appendix 7B. Ofgem is proposing to discuss the implications of Option 2A for the licence through DISG meetings. Ofgem welcomes views on this issue.

Price controls and incentive arrangements

September document

4.102. Ofgem invited views on the following price control issues:

- Ofgem's conclusion not to reopen the price control but to place incentives on the NTS and DN-GTs to encourage efficient investment decisions by the NTS and DNs²⁴;
- Ofgem's indication that the initial duration of the incentive scheme for DNs should be for one year only. These incentive arrangements will be supplemental to the price control and will be considered in detail in a separate consultation document; and
- the introduction of a "safety net" to ensure that customers are protected in the event that costs exceed benefits.

Respondents' views

4.103. In total nine respondents commented on this issue. Three shipper/suppliers and NGT supported Ofgem's conclusion that it would not be appropriate to reopen Transco's price control because of DN sales. In contrast, one shipper/supplier stated that this conclusion should be reconsidered, given that the details of the arrangements that would be implemented in the event of DN sales occurring are becoming clearer. This shipper/supplier specifically considered that the interaction between the price control and the requirement for incentives on network owners should be considered in more detail.

²⁴ Ofgem (initially) stated that it was not planning to re-open the price control in: National Grid Transco – Potential sale of network distribution businesses, Next steps, December 2003.

4.104. Three shipper/suppliers and two potential purchasers commented directly on the need to develop incentive schemes for network owners. These respondents welcomed Ofgem's intention to issue a separate consultation document on incentives. One potential purchaser specifically welcomed Ofgem's proposal that the DN incentive scheme should (initially) be one year in duration. One shipper/supplier emphasised that the incentive schemes defined for network owners should not be unduly complicated.

4.105. There was very little comment from respondents on the issue of the proposed "safety net". One shipper/supplier that did raise this issue, expressed support for the proposal. This shipper/supplier stated explicitly that the safety net should be retained until the DN sales process has been concluded.

Ofgem's proposals

4.106. Ofgem continues to be of the view that:

- ◆ the price control should not be reopened, but that incentives should be placed upon the NTS and DN-GTs to encourage efficient investment decisions;
- ◆ the initial duration of the incentive scheme for DNs should be for one year only; and
- ◆ that a "safety net" should be introduced to ensure that customers are protected in the event that costs exceed benefits and retained until the end of the process.

4.107. The proposed incentive arrangements will be supplemental to the price control and will be considered in detail in a separate consultation document.

4.108. These proposals on incentive arrangements are not included in the licence drafting in Appendix 7B. Ofgem is proposing to discuss their implications through DISG meetings, and Ofgem welcomes views on this issue.

System operator managed service agreements

September document

- 4.109. Transco intends to put in place a number of network service agreements (NSAs) between Transco's DNs and the NTS following the sale of the IDNs. The workgroups have considered whether it would be appropriate to regulate the NSAs, and in particular whether system operator managed service agreements (SOMSAs) should be regulated by Ofgem.
- 4.110. SOMSAs were designed as an interim measure to facilitate DN sales, on the assumption that in the medium to longer term, DN owners would put their own arrangements in place.
- 4.111. Ofgem's initial view, as put forward in the workgroups and in the September document, is that these agreements should be unregulated because:
- ◆ the current price control arrangements ensure that customers are protected from payments recovered by Transco from DN-GTs under the SOMSA;
 - ◆ the charges and liabilities arising from the SOMSAs should impact on the price that buyers are prepared to pay for the networks. Therefore, for the duration of this price control, the financial flows under the SOMSAs from the DN to Transco and the price paid for the network by new DN owners to Transco should net off so that there is no net financial gain by either party in transaction; and
 - ◆ regulation of the SOMSAs may tend to perpetuate the arrangements. Ofgem's roles and responsibilities RIA concluded that it was appropriate for the DN owners to be responsible for the operation of their networks. As discussed, in the short term, the DNs will discharge this responsibility through the SOMSAs. However, in the medium term, it is envisaged that DN-GTs undertake their own system operation activities in line with their responsibilities. Ofgem is concerned that, were the SOMSAs to be regulated, it may encourage these arrangements to persist longer than is desirable.

Respondents' views

- 4.112. Eleven respondents commented on this issue. One shipper/supplier and NGT suggested that SOMSAs should not be regulated. The Gas Industry Safety Group stated that only NSAs which underpin safety and emergency response arrangements should be regulated. Two shipper/suppliers expressed concerns about non-regulation if the SOMSAs extend into the longer term. A potential purchaser stated that those NSAs which are enduring, such as call handling, should be regulated.
- 4.113. Whilst the potential purchasers were broadly in favour of non-regulation, one noted that system operator managed services were a critical service for the DNs and any failure or disputes in this area may have a significant impact on customers' interest. Therefore whilst this potential purchaser supported Ofgem's position that nothing should be done which perpetuates SOMSAs, it stated that Ofgem should establish a limited degree of regulatory oversight while the SOMSAs are in place. It was suggested that this could take the form of a time-limited obligation on Transco to provide the service on a non-discriminatory basis on reasonable terms.
- 4.114. Two shipper/suppliers considered that SOMSAs should be regulated (particularly if these agreements were to persist into the long term). Energywatch agreed that SOMSAs should be regulated so that an incentive to shift costs toward such regulated activities is not created.

Ofgem's views

- 4.115. Following consideration of respondents' views, Ofgem continues to consider that it is not appropriate to regulate SOMSAs. These contracts are commercial contracts between the IDNs and the RDN business which the buyers have signed up to as part of the commercial arrangements associated with buying the DN and it is therefore not appropriate for these contracts to be regulated. However, Ofgem notes that the revenues of DN businesses are, and will continue to be, regulated. Given that Ofgem is not proposing to reopen the current price control, charges to customers will not be affected in the period to 1 April 2008.

- 4.116. It is not our expectation that the SOMSAs will remain in place in the long term but that IDNs are expected to set up their own control rooms to operate the IT/IS in approximately 18 months²⁵. However, if this is not the case and these contracts continue into the long term Ofgem will reconsider this issue and, if appropriate, regulate these agreements.
- 4.117. As it is not Ofgem's intention to regulate these SOMSAs, it will be necessary to adjust the cap for the RDN licensee in relation to de-minimis businesses (amending the current provisions within what is currently Special Condition 2: Restriction on Activity and Financial Ring fencing) for the pre-specified period for which these contracts are expected to be in place.
- 4.118. The amendments to Standard Special Condition A36 - Restriction on Activity and Financial Ring-fencing are included within special conditions specific to the RDNs (Special Condition E1: Amendments to Standard Conditions and Standard Special Conditions applicable to the licensee), which are discussed further in Chapter 6. Ofgem is currently in discussions with NGT regarding quantification of the adjustments required and the appropriate period to be applied and, as such, the drafting provided in Appendix 7B of these conditions has left these areas blank.
- 4.119. Ofgem recognises that the NSA relating to "call handling" is intended to be enduring. This agreement is an essential part of the emergency services contract and hence is already covered by Standard Special Condition A8 Emergency Services and Enquiry Obligations (formerly Amended Standard Condition 6). The revenue that Transco receives in respect of this agreement is therefore regulated.
- 4.120. Ofgem invites respondents' views on this issue.

Standards of performance

- 4.121. In this section, we consider key issues that relate to standards of performance in the event of DN sales. The key issues fall under two main headings:

- ◆ customer survey obligation; and

²⁵ It is noted that this is dependent on approval of the safety cases by the HSE.
Office of Gas and Electricity Markets

- ◆ connections.

4.122. These are considered in turn below.

Customer survey obligation

4.123. Transco currently conducts a survey of all customers who have been voluntarily and involuntarily interrupted. However, this is not a licence obligation upon Transco.

4.124. This issue was not recognised by the September document, however, following discussions at DISG, it was agreed that this practice should continue following DN sales. Ofgem is therefore proposing to introduce provisions that oblige all DN-GTs to conduct such a survey and publish the results on their web-site.

4.125. Ofgem would welcome respondent views on this proposal.

4.126. This is discussed in further detail in Chapter 5 and is incorporated within Standard Special Condition D9 - Distribution Network Incentive Scheme and Performance Reporting in Appendix 7B, which is an amended version of what was formerly Special Condition 36.

Connections

4.127. Ofgem has identified the need to introduce a new obligation on DN-GTs in relation to connections. This was not recognised at the time of the September document, but has subsequently been discussed with the DISG.

September document

4.128. Ofgem's predecessor, Ofgas, started receiving complaints in respect of anti-competitive behaviour / poor service provision by Transco from IGTs, independent connection providers and shippers during 1997/1998. In February 1999 Ofgas found Transco guilty of contravention of section 9(2)(a) of the Gas Act and paragraph 1 of condition 11 of the GT licence. Ofgas made an enforcement order imposing standards of service in respect of connection services to the customer types mentioned above. To avoid making payments Transco had to hit a target of 90% in relation to particular categories of customer. Transco had to compensate individual customers where its

performance in respect of that customer fell below 80%. Transco has also “voluntarily” refunded all customers that had obtained connections direct from Transco 10% of their connection charges from 1 March 1996 – February 1999.

- 4.129. In April 2002 Ofgem received complaints from Exoteric Gas Solutions (EGS), which had been one of the companies that previously complained about Transco. During 2003, Transco’s connections performance (provided by Fulcrum Connections, a wholly owned NGT subsidiary) deteriorated and consultation undertaken by Ofgem indicated that Transco’s performance was poor. During 2003 Transco paid out nearly £3m in compensation to customers under the terms of the original enforcement order. In May 2004 the Authority confirmed that it found Transco in contravention of section 9(1)(a) of the Gas Act and imposed a penalty of £1m.
- 4.130. Ofgem is considering the need for a new standards of service regime for connections, and consulted in April in this regard.²⁶
- 4.131. Given that, as a result of DN sales, the provisions of the enforcement order in place with Transco plc will not automatically apply to DN buyers, a new licence condition is required to ensure continued protection for connections customers connected to all DNs. This is considered to be particularly relevant given that Fulcrum will continue to provide connections services on behalf of IDNs in the short term.

Respondents’ views to the April consultation

- 4.132. Responses to the April consultation document referred to above supported reform of the enforcement order, including extension of protection to all customers rather than just the customer groups protected by the enforcement order, a move to guaranteed standards and improved accuracy / audit arrangements. A prospective buyer stated that it would be unfair to penalise the new DN owners for Transco’s past behaviour.
- 4.133. Whilst the September document did not explicitly request views from respondents on this matter, one respondent noted previous instances of anti-

²⁶ Ofgem 77-04 – Improving Transco’s provision of gas connection services: consultation on revocation of the 1999 Gas Act enforcement order and modification of Transco’s gas transporter licence.

competitive behaviour and stated that the threat to competitors in connections markets is very real.

Ofgem's proposals

- 4.134. Ofgem notes that, as a result of DN sales, a new licence condition will be required to ensure that appropriate protection for customers requiring connections is in place for all DN-GTs in the event of DN sales.
- 4.135. Ofgem is proposing to implement the changes to the enforcement order (as consulted upon) at the same time as these DN sales related changes are made. Because Transco's poor performance has affected all categories of customer, and not just those presently covered by the enforcement order, Ofgem proposes that the new regime should protect all customers except those that are in a reasonable position to benefit from competition. Ofgem proposes to introduce the new regime as follows:
- ◆ a new licence condition imposing overall standards of service in respect of connection services provided to customers currently protected by the Order. Ofgem does not have the vires to impose guaranteed standards with payments for these customers under S33AA. The licence condition will also impose requirements in terms of accuracy challenge arrangements and audit requirements, both of which featured in the 1999 order;
 - ◆ extending the existing Guaranteed Standards of Performance Regulations made via statutory instrument (SI) under S33AA of the Gas Act to impose guaranteed standards in respect of all gas transporters provision of new / altered connections to end domestic / non-domestic customers. These standards will apply to quotations and attendance on site;
 - ◆ Transco has agreed to introduce a voluntary scheme that will effectively apply the guaranteed standards imposed under S33AA to the customer groups covered by the overall standards to ensure that they are not disadvantaged by the limitations imposed by S33AA; and
 - ◆ Although the new licence condition and SI will not come in to force until the time of DN sales, Ofgem proposes that the new arrangements be

introduced on the basis of a formal undertaking from Transco as early as March in conjunction with revocation of the order. Transco has agreed that it will support the early introduction of the new regime. This will allow the new arrangements to be established in advance of DN sales.

4.136. The drafting of the new licence condition required is discussed in further detail in Chapter 6.

Business separation

4.137. In this section, we consider key issues that relate to business separation requirements in the event of DN sales. The key issues fall under two main headings:

- ◆ conditions requiring the separation of competitive and monopoly activities including separation between NTS and DN-GTs and their related IGT businesses; and
- ◆ conditions requiring the separation of Transco's NTS and RDN businesses.

4.138. These are considered in turn below.

Separation of monopoly and competitive activities

September document

4.139. In the September document, Ofgem expressed the view that amendments to the business separation provisions could be required to deal with any potential competition issues which may arise when issues arising from the identity of potential purchasers had been fully considered. We suggested that this could involve the introduction of business separation requirements modelled on those that apply to electricity distribution network operators (DNOs).²⁷

²⁷ Ofgem, *Potential sale of gas distribution network businesses –Initial thoughts on restructuring of Transco plc's Gas Transporter Licences*, Consultation Document September 2004, pg 81.

Respondents' views

- 4.140. A range of respondents, including shipper/suppliers, raised concerns regarding the potential for purchasers of DNs to obtain an unfair advantage in competitive gas shipping and supply activities. In addition, IGT representatives expressed concern that the new DN owners could unduly discriminate in favour of related IGT businesses to the detriment of other IGT businesses.
- 4.141. SSE noted that it has relevant interests and agreed with Ofgem that it would be appropriate to model any separation requirements on the framework that applies in the electricity sector. SSE also expressed the view that future business separation provisions should apply as standard special conditions to all DNs and the NTS as the principles are equally relevant to all such licensees.

Ofgem's proposals

- 4.142. Having considered respondents' views, Ofgem continues to consider that it is appropriate to update the business separation requirements to align the gas business separation requirements with those that apply in the electricity industry.
- 4.143. At a high level, the electricity regime requires DNOs to:
- ◆ put in place managerial and operational systems which prevent any relevant supplier or shipper from having access to confidential information; and
 - ◆ manage and operate the transportation business in a way that does not restrict, prevent or distort competition.
- 4.144. In addition, licensees are required to have in place a statement describing the practices, procedures and systems it has adopted to ensure that these conditions are met. The proposed conditions are discussed in more detail in Chapter 6.
- 4.145. In relation to separation of NTS and DN GT from affiliated IGTs, Ofgem considers that the non-discrimination provisions within the existing regime, including the provisions in Standard Special Condition A6, together with

Ofgem's wider competition powers are sufficient to address such concerns.²⁸

However, Ofgem welcomes respondents' views on this issue.

Separation of NTS and RDNs

September document

- 4.146. The September document reflected the Authority's position on business separation as set out in the Offtake Arrangements Conclusions Document.²⁹ This document indicated that the Authority was minded to require Transco to undertake legal separation and targeted structural separation.

Respondents' views

- 4.147. Six respondents submitted comments in relation to business separation in the context of Amended Standard Condition 39. These included three potential purchasers, two shippers and a further respondent. Of these, all were supportive of the proposals to amend this condition to ensure that no party would be able to discriminate in favour of a related business.
- 4.148. Transco expressed support for an approach to structural separation which is broadly consistent with the electricity DNO licence conditions. In setting out this view, Transco suggested that in practice the scope for undue discrimination from network monopoly to network monopoly is considerably less than between a competitive supply business and a network monopoly.

Ofgem's proposals

- 4.149. As explained in Chapter 2, the Authority has reviewed its "minded to" decision on legal separation as a result of issues associated with its implementation. Ofgem has developed a set of licence obligations that are designed to address the issues arising as a consequence of the Authority decision not to require legal separation.

²⁸ This issue is discussed further in Chapter 5 - Amended Standard Condition 4D (proposed Standard Special Condition A6).

²⁹ Ofgem, *Potential sale of gas distribution networks businesses – Offtake Arrangements Conclusions document on framework*, August 2004, pgs 46-48.

4.150. The Authority's views in relation to targeted structural separation, which have previously been set out in the Offtake Arrangements Conclusions Document, remain unchanged. Transco would be required to have a statement in place describing the practices, procedures and systems it has adopted to ensure no undue discrimination between RDN and IDN businesses. In particular, the statement would set out how and to what extent Transco would maintain informational, operational and physical separation between the NTS and RDN businesses so as to prevent any breach of the requirement for no undue discrimination by the NTS.

4.151. These new licence conditions are discussed further in Chapter 6.

Treatment of LNG and metering

Background

4.152. Within its September licence consultation Ofgem detailed that NGT was of the opinion that:

- ◆ the most appropriate location for the licence obligations relating to LNG Storage should be Transco's NTS-GT licence only in view of the fact that such facilities are connected to the NTS; and
- ◆ any metering obligations retained should be retained in both NTS and DN-GT licences.

Respondents' views

4.153. Eight respondents commented on the issue of the provisions relating to LNG Storage. Two shipper/suppliers, two potential purchasers and NGT expressed support for these provisions to apply to the NTS alone. However, a shipper/supplier commented that although operational and financial issues are currently evident in relation to LNG sites, these would need to be assessed against the future concept of separation between the NTS and DNs.

4.154. Concerns were raised by one shipper/supplier with respect to the development of provisions to accommodate LNG import facilities and the fact that this was not included within the informal licence consultation.

- 4.155. One DISG member commented on the proposals to revert to the designated Standard wording for storage related provisions within standard special conditions applicable to DN-GTs. This respondent argued that it might be helpful to specify on-shore sites and diurnal storage in these definitions.
- 4.156. One potential purchaser stated that the metering provisions should not be applied to both NTS and DN licences. The potential purchaser stated that metering obligations should only apply to RDNs. One shipper/supplier suggested that the metering obligation should be applicable to both NTS and DN licences.

Ofgem's proposals

- 4.157. Given respondents' views, Ofgem also considers it to be appropriate for obligations relating to LNG Storage to sit within the NTS-GT licence only. We do not consider that this will affect the development of import facilities, as these provisions relate only to specific LNG facilities owned by Transco. Ofgem considers that retention of the designated standard condition wording for obligations applying to all DN-GTs is appropriate, but would welcome views from respondents on this matter.
- 4.158. As such:
- ◆ the standard special conditions applicable to both NTS and DN licensees will revert to the references to storage facilities contained in the standard conditions designated by the Secretary of State under the Utilities Act;
 - ◆ licence conditions that relate exclusively to LNG Storage are NTS Special licence conditions i.e. Special Condition C3 - Restriction of Prices for LNG Storage Services; and
 - ◆ Ofgem is proposing a new special condition upon the NTS, which seeks to "augment" standard special conditions as appropriate.
- 4.159. This new "augmenting" provision (Special Condition C1 – Amendments to Standard Conditions and Standard Special Conditions applicable to the licensee relating to LNG) is discussed further in Chapter 6.

4.160. Following consideration of respondents' views with respect to metering, Ofgem considers that obligations relating to metering should sit within both NTS and DN-GT licences as both will need to undertake metering activities (or be responsible for arranging metering services).

4.161. Ofgem invites respondents' views on these issues.

5. Existing Transco plc Licence conditions

- 5.1. As set out in Chapter 3 it is proposed that the Section 23, provided in Appendix 5, will give effect to the necessary modifications to Transco plc's original GT licence and the five new additional GT licences required to separate the existing price control between the NTS and DN-GTs. Before any sale of DNs can proceed it will be necessary to modify substantially these six licences further to ensure that the provisions will be effective in any post sales world. The modifications to Transco plc's existing standard and special licence conditions are discussed in this chapter. The new licence conditions that Ofgem considers may be required in the event of any DN sale are considered in Chapter 6.
- 5.2. Ofgem has developed a draft composite licence which is intended to set out the licence obligations that NTS and DN-GTs would be subject to in any post DN sales scenario. This composite licence is attached to this document as Appendix 7. Throughout this chapter, cross references are made to these proposed licence conditions and respondents' views are invited.
- 5.3. Following consideration of respondents' views Ofgem intends to introduce these changes at the time of the Section 8AA consent (and associated additional Section 23 notice). For the avoidance of doubt, these proposed modifications would only take place should the Authority consent to any DN Sale in January 2005.
- 5.4. This chapter therefore includes:
- ◆ a brief description of each licence condition contained within Transco plc's current GT licences;
 - ◆ a high level view of the changes, proposed by Ofgem as part of the September document, in connection with a potential DN sale;
 - ◆ a summary of the responses received in relation to proposed changes to each standard and special licence condition; and
 - ◆ Ofgem's views and associated proposals in relation to each condition within Transco's original GT licence and the five new additional GT licences including the way forward.

Overview

- 5.5. This chapter follows the format of Transco plc's original GT licence and the five new additional GT licences, and therefore sets out the proposed changes (if any) to:
- ◆ Standard Conditions³⁰ (Part A, Part B, and Part C of Transco's original GT licence and the five new additional GT licences); and
 - ◆ Special Conditions.
- 5.6. The conditions described in Transco plc's original GT licence and the five new additional GT licences as "not used" are not discussed in this chapter nor are any proposed or pending modifications to such licences which are unrelated to the proposed sale of Transco's DNs.
- 5.7. Ofgem would also like to make clear that the potential sale of one or more of Transco's DNs is not a regulatory initiative, but a commercial decision taken by NGT and accordingly, the proposed modifications included in this chapter will only apply to Transco's original GT licence and the five new additional GT licences. As such, the proposed amendments will not apply to GT licences held by IGTs.
- 5.8. In issuing this document it is important to clarify that there can be no expectation on the part of NGT, Transco, potential DN purchasers, shippers, suppliers, IGTs or any other interested parties either as to what the Authority's final decision in relation to the proposed transaction may be, or as to the regulatory framework which may be implemented if the Authority consents to the proposed transaction.

³⁰ Including Amended Standard Conditions

Standard Conditions

Part A

Amended Standard Condition 1 – Definitions and interpretation

Description

- 5.9. This condition explains and defines the key terms within the licence unless the context otherwise requires.

September document

- 5.10. In the informal licence consultation, Ofgem proposed to revert this condition within the licences³¹ held by Transco plc to the designated standard condition (as designated by the Secretary of State and updated by the Authority through the CLM procedure). The designated standard condition would then apply to all GTs including NTS and DN-GTs. Ofgem also proposed that where an additional or modified definition was required these would be contained in a separate Special Condition applicable to an individual licensee or a Standard Special Condition applicable to DN GTs, NTS GTs or both.

Respondents' views

- 5.11. Ofgem received one response concerning Amended Standard Condition 1 from a gas shipper. This respondent raised wider concerns surrounding Ofgem's proposed licence structure and in particular the private CLM process. These issues are considered in Chapter 4.
- 5.12. A DISG member, representing a shipper/supplier, stated that it would be more user friendly for all definitions to be located in one place.

³¹ At the time that the September document was published Ofgem had not yet granted 5 new additional licences to Transco plc. The September document therefore referred to Transco's existing licence and any new licences granted by Ofgem. As these new additional licences have now been granted to Transco, references in this chapter, to the September document are as if the licences had been granted at the time at which the September document was published.

Ofgem's proposals

- 5.13. As set out in Chapter 4, following consideration of respondents' views, Ofgem continues to believe that it is appropriate to introduce the private CLM and associated licence structure.
- 5.14. Ofgem accepts the comment raised within DISG, that placing definitions in separate conditions may add complexity when reading the licences. However, this is necessary to ensure that, as far as possible, the definitions contained within the licences are subject to the statutory CLM procedure or the private CLM procedure. Ofgem considers that these advantages outweigh the disadvantages caused by increased complexity. Ofgem also notes that Transco's licences already contain a number of definitions outside of the Amended Standard Condition 1 and therefore, to a degree, the complexity already exists.
- 5.15. Ofgem therefore proposes to revert Amended Standard Condition 1 to the designated Standard Condition 1.
- 5.16. Ofgem also proposes to introduce a Standard Special Condition (A3. Definitions and Interpretation) for all NTS and DN GTs. This proposed condition contains new definitions as well as those that are required to supplement the existing definitions set out in Standard Condition 1. The drafting for these Conditions (Standard Condition 1 and Standard Special Condition A3) is provided for comment in Appendix 7).
- 5.17. Ofgem's proposals relating to the treatment of LNG Storage within the licences are detailed in Chapter 4. To reflect these proposals the following changes relating to Amended Standard Condition 1 are being proposed:
- ◆ in respect of the references to storage facilities, Standard Special Condition A3 has reverted to the drafting contained in the standard conditions designated by the Secretary of State under the Utilities Act; and
 - ◆ a new NTS Special Condition has been introduced to "augment" this Standard Special Condition with LNG related provisions (Special Condition C1, paragraph 1). This is discussed in further detail in Chapter 6.

- 5.18. Ofgem invites respondents' views on its proposals for Amended Standard Condition 1. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 2 – Application of Section C (transportation services obligations)

Description

- 5.19. This standard condition establishes the circumstances under which Section C of the standard conditions of a GT licence will have effect either in whole or in part, with the consent of the relevant licence holder.

September document

- 5.20. Ofgem did not propose any modifications to this condition within the September consultation and, as such, considered that Standard Condition 2 should continue to apply to all GT licensees.
- 5.21. However, Ofgem considered that there is also a need for a switch mechanism to apply to the designated standard conditions in Part A and B of the licence and the Standard Special Conditions. In this respect, Ofgem included a proposal to introduce a Standard Special Condition similar to Standard Condition 2 which would apply to these sections of the licence and enable Ofgem to switch on or off Conditions in these sections.

Respondents' views

- 5.22. Ofgem did not receive any comments in relation to this proposal.

Ofgem's proposals

- 5.23. Ofgem's views relating to its private CLM procedure are set out in Chapter 4 and the associated new conditions in Chapter 6.

- 5.24. Ofgem continues to consider that Standard Condition 2 should remain in all GT licences including NTS and DN-GTs. The wording of this Condition is provided in Appendix 7A.
- 5.25. Ofgem invites respondents' views on its proposals for Standard Condition 2. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 3. Payments by the Licensee to the Authority

Description

- 5.26. Standard Condition 3 sets out the obligation to pay to the Authority an amount determined in accordance with the Condition. It prescribes the relevant proportion of the costs of the Authority, Consumer Council, Competition Commission and Secretary of State that are attributable to the licensee and are therefore payable by it.

September document

- 5.27. Ofgem was not minded to propose any modifications to this condition as part of the informal licence consultation and, as such, intended that Standard Condition 3 would continue to apply to all GT licences, including NTS and DN-GTs.

Respondents' views

- 5.28. Ofgem received one response from a gas shipper/supplier concerning Standard Condition 3. The respondent considered that it was appropriate to consider how the charges would be shared between the NTS and DN licensees.

Ofgem's proposals

- 5.29. Ofgem continues to believe that no changes to Standard Condition 3 are necessary as part of the DN Sales process and that the condition should apply to

all GTs including NTS and DN-GTs. Ofgem agrees with the respondent who stated that relevant payments should be appropriately shared between the licensees. Standard Condition 3 is drafted such that the Licensee pays a proportion of the costs calculated by the Authority. This enables the Authority to determine the correct allocation of costs between DN and NTS-GTs and all other licence holders.

- 5.30. The wording of this Condition (Standard Condition 3) is provided in Appendix 7A.
- 5.31. Ofgem invites respondents' views on its proposals for Standard Condition 3. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Part B

Amended Standard Condition 4 – Charging Gas Shippers - General

Description

- 5.32. Amended Standard Condition 4 sets out a requirement on the licensee to provide the Authority with charging statements. The condition also requires that the licensee must use all reasonable endeavours to provide at least 150 days' notice to the Authority, in the event of a proposed change to the transportation charges. It also contains obligations relating to the charging for LNG Storage arrangements.

September document

- 5.33. In the September document Ofgem set out a number of proposals to address concerns raised by workgroup participants in relation to the potential costs arising from multiple changes to charges within a year in any post sales scenario. These included:

- ◆ **Reasonable endeavours obligation on frequency of changes:** a proposal to introduce obligations on NTS and DN-GT licensees to use reasonable endeavours not to change their gas transportation charges and/ or charging methodologies other than on a specified date each year, for example 1 October; and
- ◆ **Coordination by the Joint Office (JO):** a proposal to require all DN and NTS GTs to use the JO to administer the process on all consultations on proposed amendments to charges and/ or charging methodologies. This will enable the JO to coordinate the processes involved in relation to consultation on changes to charging methodologies and/ or charges for each NTS and/ or DN-GTs.

- 5.34. In the September document Ofgem stated that Transco was of the opinion that the most appropriate location for the licence obligations relating to LNG Storage should be Transco's NTS GT licence in view of the fact that such facilities are connected to the NTS. Ofgem invited views on this issue.
- 5.35. Given the extent of the proposed changes from the designated version of Standard Condition 4, Ofgem proposed to introduce a new Standard Special Condition (A4) containing the provisions contained in this Condition with necessary amendments that would apply to NTS and DN-GT licences. The designated Standard Condition 4 will then be switched off in the licences of NTS and DN-GTs.

Respondents' views

- 5.36. Ofgem received four responses concerning Amended Standard Condition 4. Ofgem notes that other respondents commented on these issues in response to the key issues chapter of the September document. These views are set out in Chapter 4.
- 5.37. Overall, the gas shipper/suppliers that commented on Ofgem's proposals were supportive. One gas shipper/supplier considered that more rigid requirements should be placed on NTS and DN licensees relating to valid dates and on co-ordination. This shipper/supplier considered that a failure to do so would impose unreasonable costs on users and could potentially be unworkable. A further shipper/supplier supported Ofgem's proposals for a charge change

window. This respondent additionally commented on the treatment of provisions relating to LNG storage. This is discussed in Chapter 4.

- 5.38. A potential purchaser (also with a shipping business) supported a reasonable endeavours obligation in respect of frequency of changes to charges. They stated that this would not prevent changes to charges more than once a year in the event that there was an over/under recovery of revenue under Special Condition 28B. This respondent suggested that a suitable date for alignment of charge changes was 1 April. Furthermore, the respondent offered its support for changes to charges to be administered by the Joint Office. This respondent supported NGT's preferred approach for LNG provisions to be contained only in the licence of the NTS. However the respondent did raise concerns over the proposed licence structure.
- 5.39. NGT did not support Ofgem's proposals for a charge change window. NGT considered that Ofgem's proposals would result in a greater risk of over or under recovery of revenue. NGT also set out its view that the interaction between the proposals for this, and Amended Standard Condition 4A, should be considered with other licence conditions, in particular the current penal interest rates that apply for over recovery under Special Condition 28B. NGT stated that there may be times when it is important for changes to charges to occur more frequently. NGT also set out its view that NTS charges would need to change at least four times in any year. It therefore suggested that the NTS should be excluded from any charge change window proposals. NGT offered its limited support to the Joint Office proposals, stating that these should again only apply to DN GTs. NGT also noted that if the concept of the NTS contracting with connectees for an exit product is adopted then this will need to be reflected in the licence.
- 5.40. This condition was also discussed at DISG. A DISG member, representing a shipper/supplier, stated that the condition should be strengthened so that the licensee must use 'all reasonable endeavours'. They also stated that NTS and DN-GTs should be treated in an equivalent manner. However, they acknowledged some difficulties for GTs in complying with this and suggested a 'best endeavours' obligation on a twice a year basis. A further DISG member, representing a shipper/supplier, expressed disappointment with NGT's position as they considered that these modifications had already been agreed. The

shipper/supplier representative provided their support for Ofgem's proposals and also stated that a minimum of two months' notice of any changes in charges should be given. A similar proposal was put forward by a shipper/supplier representative.

- 5.41. One DISG member, representing a potential purchaser raised an issue as to how these proposals would relate to Amended Standard Condition 48, Last Resort Payment Claims. This DISG member also requested more detail on the Joint Office arrangements and how consultation would be co-ordinated.
- 5.42. DISG members also raised comments relating to the treatment of LNG storage provisions which are discussed in Chapter 4.

Ofgem's proposals

- 5.43. Ofgem has given careful consideration to respondents' views on this amended standard condition. Ofgem has additionally developed its thinking on this condition following the decision to implement Option 2A of the offtake arrangements. Ofgem consideration on these issues is set out in Chapter 4.
- 5.44. As set out in Chapter 4, Ofgem considers that the reasonable endeavours obligation relating to frequency of changes to charges must apply to both NTS and DN-GTs particularly in view of the decision to implement Option 2A of the offtake arrangements.
- 5.45. Ofgem accepts that the reasonable endeavours obligation is subordinate to the best endeavours obligation not to exceed allowed revenue.
- 5.46. Ofgem continues to believe it appropriate for the Joint Office to administer the proposals to change these charges. The obligations regarding the Joint Office are set out in a new Standard Special Condition (A12) in Appendix 7B to this document.
- 5.47. Ofgem is therefore proposing that the provisions contained within Amended Standard Condition 4 (other than those relating to LNG storage) will be replicated in Standard Special Condition A4.
- 5.48. Standard Special Condition A4 also contains the proposals set out in Chapter 4 concerning the frequency and timing of changes to charges and the use of the

Joint Office. It is therefore proposed that the following provisions will apply to NTS and DN-GTs:

- ◆ that the licensee shall use its reasonable endeavours not to make any changes to charges or reserve prices governed by this condition more frequently than **twice** in a formula year;
- ◆ that the licensee shall use its reasonable endeavours only to make changes to charges or reserve prices governed by this condition on 1 April and 1 October in each formula year; and
- ◆ that the licensee shall comply with the Joint Office Arrangements for the administration of any proposals.

5.49. The drafting for this Condition (Standard Special Condition A4) is provided for comment in Appendix 7.

5.50. As discussed in Chapter 4, to address the issue of LNG:

- ◆ this standard special condition has reverted to the references to storage facilities contained in the standard conditions designated by the Secretary of State under the Utilities Act; and
- ◆ a new NTS Special Condition has been introduced to “augment” this standard special condition with LNG related provisions (Special Condition C1, paragraph 2). This is discussed in further detail in Chapter 6.

5.51. Ofgem invites respondents’ views on its proposals for Amended Standard Condition 4. Following consideration of respondents’ views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be consulted upon in February 2005. Further consultation may take place during this period through the DISG meetings.

Amended Standard Condition 4A – Obligations as Regards Charging Methodology

Description

- 5.52. This amended standard condition describes the objectives of a charging methodology and sets out that the transporter should, from time to time, make modifications to facilitate the achievement of these objectives.

September document

- 5.53. As part of the informal licence consultation, Ofgem detailed that modifications would be necessary to this amended standard condition to accommodate:

- ◆ the creation of a reasonable endeavours obligation on frequency of changes to the charging methodology and to ensure that such changes are effected on a specified date in the year (for instance, 1 October);
- ◆ the involvement of the JO in the process for amending the methodologies; and
- ◆ an obligation on NTS and DN-GT licence holders to keep the charging methodology under review at all times to ensure that there is coordination, consistency and best practice in the achievement of the relevant objectives.

- 5.54. Given the changes required to the designated version of Standard Condition 4A, Ofgem proposed to introduce a new Standard Special Condition (A5) containing the provisions of this condition to apply to NTS and DN-GT licences.

Respondents' views

- 5.55. Ofgem received four responses relating to Amended Standard Condition 4A.
- 5.56. One gas shipper/supplier and an IGT expressed support for the proposal to limit the frequency under which transporters would be permitted to implement changes to their charging methodologies to avoid unreasonable costs. The shipper/supplier raised the issue of whether IGTs should also be covered through these provisions.

- 5.57. A potential purchaser suggested that it would be appropriate for transporters to keep their charging methods under review and make amendments from ‘time to time but no less than annually’. The purchaser considered that this obligation would require review frequently enough to ensure consistency of approach but without involving constant consultation and review. This potential purchaser also stated that it was unclear as to why it was necessary to have requirements regarding frequency of changes in relation to the methodology as well as to the charges.
- 5.58. NGT set out the same views as with Amended Standard Condition 4. They also suggested that there should be a review of the differences in the test for the modification of the charging methodology between the electricity and gas licence³².
- 5.59. DISG members discussed this condition. Overall the comments provided were as those set out above for Amended Standard Condition 4. However, the following additional comments were provided:
- ◆ one DISG member, representing a gas shipper/supplier, stated that the provisions within Amended Standard Condition 4A relating to auctions should be removed from DN-GT licences;
- 5.60. a further DISG member, representing a shipper/supplier, provided its support for Ofgem’s proposals to introduce an obligation to keep the charging methodology under review at all times. This DISG member also set out that it was important that the implementation of changes to charges occurred at the same time as changes to the charging methodology;
- ◆ a DISG member, representing a potential purchaser, stated that the obligation to keep methodologies under review at all times was unreasonable; and

³² Condition C7A of the electricity transmission licence requires the licensee to make modifications to the charging methodology as may be requisite for the purpose of *better achieving* the relevant objectives. Under the current transporters licence (and as proposed for Standard Special Condition A5 the licensee is required to make changes as may be requisite for the purpose of *achieving* the relevant methodology objectives.

- ◆ DISG members also commented that IGTs should be covered through this provision.

Ofgem's proposals

- 5.61. Following consideration of respondents' views and implications of the decision to implement Option 2A for offtake arrangements, Ofgem considers that the reasonable endeavours obligation should be changed such that it requires licensees to use reasonable endeavours to announce and implement changes to the methodologies on two specified dates in the year. We consider it appropriate to repeat the restriction on frequency of changes obligation in respect of the methodology to ensure that there is further protection for shippers in relation to the number of methodology changes and to ensure that methodology changes between GTs are conducted at the same times in the year to enable the proposals to be administered effectively by the Joint Office and mitigate the shippers' costs of scrutinising these proposals.
- 5.62. Ofgem continues to consider it appropriate for the licensee to be required to use the JO to administer the process for consultation on changes to the charging methodologies to ensure that changes are widely consulted on, and that the consultation process is consistent with other DN and/ or NTS-GTs who are also consulting on changes to methodologies.
- 5.63. In relation to the obligation to keep the charging methodology at all times under review, Ofgem considers it appropriate to change its proposals such that the licensee is required to keep the charging methodology at all times under review for the purposes of meeting the relevant objectives. The words to achieve "co-ordination, consistency and best practice" in meeting the relevant objectives will therefore be removed. Ofgem is concerned that these words could imply co-ordination between GTs in relation to the content of the charging methodologies and the achievement of the relevant objectives, which is clearly inappropriate.
- 5.64. Ofgem does not agree with the comments raised at DISG that the obligation to keep the charging methodology at all times under review is too onerous and could require active compliance 24 hours a day. It is important the obligations regarding the charging methodologies are ongoing and therefore we do not support the proposal put forward by a prospective buyer that the obligation

should be to review the methodology “from time to time”. We consider that the drafting proposed by Ofgem sends the right message that the obligation to review the methodology is ongoing. We also consider that it is possible for the licensee to comply with this obligation without having to consider its charging methodology 24 hours a day. Ofgem notes that the drafting is intending to mirror the provisions within the electricity transmission licence and notes that electricity licensees have not experienced problems of the nature suggested by the DISG respondent.

- 5.65. In respect of the point raised by NGT regarding the differences in the test for the making of modifications to the electricity charging methodologies and gas charging methodologies (i.e. the *better achievement* of the relevant objectives in electricity as opposed to the *achievement* of the relevant objectives in gas), Ofgem’s current proposal is that we retain the wording currently contained in Transco’s licence. However, we would be interested in the views of respondents on this issue.
- 5.66. In respect of the other points raised by respondents and DISG members, Ofgem considers that it would not be best regulatory practice to seek to extend the reasonable endeavours obligations relating to the frequency of changes to charges and/or charging methodologies to the IGTs through the DN Sales process. The number of possible changes to IGTs charges is not affected by the sale of Transco’s DNs.
- 5.67. We do not consider it necessary to remove the wording relating to auctions from the licence conditions applicable to DNs. The wording only applies when the charges are affected by auctions.
- 5.68. In view of the scope of changes to this condition it is proposed that Standard Special Condition A5 will be introduced into the licences of all DN and NTS-GTs containing the provisions of the condition including the changes outlined in this chapter. Amended Standard Condition 4A will then revert to the designated standard condition in the licences of all DN and NTS-GTs and will be switched off in these licences. The drafting for this Condition (Standard Special Condition A5) is provided for comment in Appendix 7B.
- 5.69. As discussed in Chapter 4, to address the issue of LNG:

- ◆ this standard special condition has reverted to the references to LNG storage facilities contained in the standard conditions designated by the Secretary of State under the Utilities Act; and
- ◆ a new NTS Special Condition has been introduced to “augment” this standard special condition with LNG related provisions (Special Condition C1, paragraph 3). This is discussed in further detail in Chapter 6.

5.70. Ofgem invites respondents’ views on its proposals for Amended Standard Condition 4A. Following consideration of respondents’ views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 4B – Connection Charges etc

Description

5.71. This condition permits the relevant transporter, in relation to the connection of premises to the main, to charge the person whose premises are being connected for the costs of supplying and laying the pipe.

September document

5.72. As part of the informal licence consultation Ofgem was minded not to propose any modifications to this condition and, as such, intended that Standard Condition 4B would apply to all GT licences.

Respondents’ views

5.73. Ofgem received 2 responses concerning its proposals for Standard Condition 4B. Two respondents supported the proposals regarding Standard Licence Condition 4B. A shipper raised a point relating to the Designated Registrar of Pipes which is considered under Standard Condition 33 below.

- 5.74. A DISG member, representing IGTs, raised a concern surrounding the effect of DN Sales on competition in connections. It was suggested that a new licence condition is appropriate.

Ofgem's proposals

- 5.75. Having considered respondents' views Ofgem continues to propose not to make any changes to this condition and therefore that this condition will apply to all GTs including DN and NTS-GT licence holders. The wording of this Condition (Standard Condition 4B) is provided in Appendix 7B.
- 5.76. In respect of the point raised regarding the need for a new licence condition on competition in connections, Ofgem is proposing that a new licence conditions setting out standards of service for connections is introduced (Standard Special Condition D10, Provision of Connections Information). Ofgem's proposals regarding this are set out in Chapter 6.
- 5.77. Ofgem invites respondents' views on its proposals for Amended Standard Condition 4B. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be consulted upon in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 4C – Charging of Gas Shippers – Supplemental Connection Charges

Description

- 5.78. Standard Condition 4C permits the licensee to include 'supplementary charges' in its charges for the conveyance of gas to premises in areas designated by the Authority which have not previously been supplied by gas or are not within 23 metres of a relevant main. This condition is expressly time limited in application (applications for designation had to be received by 31 December 2003).

September document

- 5.79. In the September document, Ofgem stated that it was minded to retain this condition in the NTS and DN-GT licences but to switch it off as the time limit for receipt of application has now passed.

Respondents' views

- 5.80. Ofgem received two responses concerning its proposals for Standard Condition 4C. Both supported the removal of the condition. However, one of the respondents (a potential purchaser) stated that this modification was not part of the DN sales process and therefore should be addressed at a later date.

Ofgem's proposals

- 5.81. Ofgem acknowledges that its proposals for Standard Condition 4C do not directly relate to DN Sales. However, Ofgem continues to believe that it is desirable as part of this process to remove time expired conditions to give clarity to licensees (particularly any new purchasers of DNs) as to the obligations within their licence. Ofgem therefore intends to switch off this condition and switch this condition off in the licences of other GTs at a suitable opportunity.
- 5.82. Ofgem invites respondents' views on its proposals for Amended Standard Condition 4C. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Amended Standard Condition 4D – Conduct of Transportation Business

Description

- 5.83. This condition obliges the licensee to conduct its transportation business to ensure that neither it, nor any affiliate or related undertaking, or any gas shipper/supplier or supplier receives any unfair commercial advantage including any such advantage from a preferential or discriminatory arrangement. The

definition of transportation business within this condition includes LNG Storage, metering services and meter reading services.

September document

- 5.84. In the September document, Ofgem requested views regarding the provisions of this Condition and, in particular, whether metering and LNG Storage arrangements should apply to the NTS and DN-GT licences. Ofgem proposed that a new standard special condition containing the provisions in this condition should be implemented to apply within the NTS and DN-GT licences.
- 5.85. Ofgem also set out that this condition, in conjunction with other conditions in the GT licence, may require further modification to deal with any potential competition issues which may arise once the implications of the potential purchasers' identities have been considered.

Respondents' views

- 5.86. Ofgem received one response concerning Amended Standard Condition 4D. The respondent, representing a potential purchaser, agreed that the modifications to support competition should be considered at a later stage of the DN sales process. The respondent also considered at this stage that it would not be necessary to include further obligations within this licence condition.
- 5.87. A DISG member discussed whether the requirements relating to metering and meter reading services should apply to both the NTS and DN-GTs. Two shipper/supplier representatives were keen to ensure that the current arrangements on the NTS remain in place.
- 5.88. Some DISG members, representing IGTs, expressed concern that there could be competition issues between any NTS or DN GT also owning, within the same group, an IGT business.

Ofgem's proposals

- 5.89. Ofgem continues to propose that Amended Standard Condition 4D is replaced by Standard Special Condition A6 which would apply to NTS and DN-GTs.

- 5.90. Having considered respondents' views including DISG members, Ofgem considers that it is appropriate for the provisions relating to metering services and meter reading services to apply both to the NTS and DN-GTs. This is reflected in the drafting of Standard Special Condition A6 and discussed in Chapter 4.
- 5.91. The drafting for this Condition (Standard Special Condition A6) is provided for comment in Appendix 7B. This condition is "augmented" by NTS Special Condition C18 (Conduct of the Transportation Business in respect of the NTS) to prevent the NTS from conferring unfair commercial advantages on its RDNs.
- 5.92. As discussed in Chapter 4, to address the issue of LNG:
- ◆ this standard special condition has reverted to the references to LNG storage facilities contained in the standard conditions designated by the Secretary of State under the Utilities Act; and
 - ◆ a new NTS Special Condition has been introduced to "augment" this standard special condition with LNG related provisions (Special Condition C1, paragraph 4). This is discussed in further detail in Chapter 6.
- 5.93. Ofgem notes the concern of the DISG members, representing IGTs' surrounding the potential competition issues between any NTS or DN-GTs also owning, within the same group, an IGT business. Ofgem considers that the provisions within the proposed Standard Special Condition A6 together with Ofgem's wider competition powers are sufficient to address such concerns. However, Ofgem welcomes respondents' views on this issue.
- 5.94. Ofgem has not identified the need for any further modifications to address competition concerns within this condition to deal with potential purchasers owning both competitive and monopoly activities within the same group. Again, Ofgem invites respondents' views on this issue.
- 5.95. Ofgem invites respondents' views on its proposals for Amended Standard Condition 4D. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales

then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Amended Standard Condition 4E – Requirement to Enter into Transportation Arrangements in Conformity with the Network Code

Description

- 5.96. This condition requires the licensee to enter into transportation arrangements that conform with the relevant provisions of the Network Code, unless the Authority accepts otherwise. For the purposes of this condition transportation arrangements include LNG Storage arrangements. This condition also includes an obligation on the licensee concerning information disclosure.

September document

- 5.97. Ofgem proposed, within the informal licence consultation, that this condition would need to be amended to reflect new commercial arrangements. It set out that two approaches were being considered within the workgroups with respect to the governance of these arrangements (i.e. UNC only approach or UNC plus offtake code). These are discussed in more detail in Chapter 4.
- 5.98. Ofgem therefore proposed that there were three areas where modifications would likely be required to Amended Standard Condition 4E. These are set out below:
- ◆ a standard special condition may be required for all NTS and DN-GT licensees to require them to enter into transportation arrangements in accordance with the UNC;
 - ◆ a special condition may be required in the NTS-GT licence to accommodate LNG Storage arrangements; and
 - ◆ a standard special condition may be required for both the NTS and DN-GT licensees containing an obligation to accede to, and comply with any, offtake code arrangements.

Respondents' views

- 5.99. The respondents' views on this condition relating to the proposal to have a separate Offtake Code as well as a UNC are set out in detail in Chapter 4 of this document.
- 5.100. Ofgem received no responses concerning the specific provisions in Amended Standard Condition 4E.

Ofgem's proposals

- 5.101. Given Ofgem's proposals set out in Chapter 4 that there is no need for a separate Offtake Code, there are limited changes required to this condition.
- 5.102. Ofgem believes that the amendments in Transco plc's existing GT licences to Standard Condition 4E relating to information disclosure should apply to NTS and DN-GTs. Ofgem is therefore proposing that Standard Special Condition A7 is introduced to all NTS and DN-GT licences. The drafting for this Condition (Standard Special Condition A7) is provided for comment in Appendix 7B.
- 5.103. As discussed in Chapter 4, to address the issue of LNG:
- ◆ this standard special condition has reverted to the references to LNG storage facilities contained in the standard conditions designated by the Secretary of State under the Utilities Act; and
 - ◆ a new NTS Special Condition has been introduced to "augment" this standard special condition with LNG related provisions (Special Condition C1, paragraph 5). This is discussed in further detail in Chapter 6.
- 5.104. Ofgem invites respondents' views on its proposals for Amended Standard Condition 4E. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be consulted upon in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 5 – System Development Obligations

Description

- 5.105. Standard Condition 5 requires that a licensee applying for an extension of its licence under section 7(4) of the Gas Act must give notice to the HSE and (if required) the Designated Registrar of Pipes.

September document

- 5.106. As part of the informal licence consultation, Ofgem was minded not to propose any modifications to this condition and, as such, Standard Condition 5 would continue to apply to all GT licences including NTS and DN-GTs.

Respondents' views

- 5.107. Ofgem received two responses concerning its proposals for Amended Standard Condition 5. NGT agreed that this condition needed to apply to both NTS and DN-GTs and did not consider that any confidentiality issues would arise. The Gas Industry Safety Group offered its support to Ofgem's proposals to retain this condition and that it should apply to both NTS and DN-GTs.

Ofgem's proposals

- 5.108. Following consideration of respondents' views on this condition Ofgem continues to consider it appropriate for Standard Condition 5 to continue to apply to all GT licences including NTS and DN-GTs. The wording of this Condition (Standard Condition 5) is provided in Appendix 7A.
- 5.109. Ofgem invites respondents' views on its proposals for Standard Condition 5. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be consulted upon in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 5A – Information to be Provided to the Designated Registrar of Pipes

Description

- 5.110. Subject to the condition becoming applicable (by the Authority issuing a direction), this condition describes the information that the licensee is obliged to provide to the Designated Registrar of Pipes within 28 days of commissioning a new main or changing existing data. This condition requires the licensee to give 7 days notice to the registrar of the location of a pipe before it is commissioned.
- 5.111. There is currently no designated registrar of pipes.

September document

- 5.112. Ofgem detailed within the informal licence consultation that, subject to consideration of the responses received, it was minded not to propose any modifications to this condition and therefore Standard Condition 5A would continue to apply to all GT licences.

Respondents' views

- 5.113. Ofgem received two responses to its proposals concerning Standard Condition 5A. Both respondents supported this proposal. A potential purchaser accepted the need to retain the Designated Registrar of Pipes but stated that this should not be appointed during the DN Sales process. The potential purchaser also stated its view that consideration of these issues should be primarily a matter for the HSE.

Ofgem's proposals

- 5.114. Ofgem continues to consider it appropriate to make no changes to this condition and therefore that it should apply to all GTs including NTS and DN licence holders. The issue as to whether Ofgem will be issuing a direction activating the Designated Registrar of Pipes provisions of the licence is considered in the section on Standard Condition 33 below.
- 5.115. The wording of this Condition (Standard Condition 5A) is provided in Appendix 7A.

5.116. Ofgem invites respondents' views on its proposals for Standard Condition 5A. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be consulted upon in February 2005. Further consultation may take place during this period through the DISG meetings.

Amended Standard Condition 6 – Emergency Services and Enquiry Service Obligations

Description

5.117. Amended Standard Condition 6 sets out a number of obligations on the licensee with respect to emergency services. These include:

- ◆ **telephone service.** A requirement that the licensee must establish or procure the establishment of and operate and maintain a single free of charge, efficiently run, well publicised, continuously manned emergency telephone number, including arrangements for the deaf and blind;
- ◆ **domestic supplies and minor repairs.** A requirement to prevent gas escapes in such a way as to maintain as far as reasonably practicable the supply to domestic premises for heating and cooking; and
- ◆ **requirements on personnel.** A requirement for work to be completed by trained persons able to recognise leakage of carbon monoxide who will inform the owner or the occupier about the carbon monoxide risks.

5.118. There is also a statutory obligation on Transco to provide the telephone service.

September document

5.119. Within the informal licence consultation Ofgem proposed that this Amended standard condition should become a Standard Special Condition (A8)

applicable to NTS and DN GT licences³³ to accommodate changes to the designated condition within Transco's licence.

Respondents' views

- 5.120. Ofgem received seventeen responses concerning Amended Standard Condition 6.
- 5.121. A number of respondents raised issues relating to emergency services in the three areas highlighted by Ofgem in the September document (i.e. at DN boundaries, provision of emergency services to IGTs, and provision of emergency services to the NTS). These comments are set out in detail in Chapter 4.
- 5.122. A number of points were made relating to the general handling of emergencies post DN Sales. These included:
- ◆ One respondent stated that an integrated and consistent response for emergency situations should be a fundamental pre-requisite for any DN Sales;
 - ◆ A potential purchaser stated that important concerns over safety will be addressed in part by careful definition of responsibilities. Overall it was supportive of Ofgem's proposals.
- 5.123. One respondent provided its support for Ofgem's proposal relating to Amended Standard Condition 6 and additionally considered that the scope of the condition should be expanded.
- 5.124. The Gas Industry Safety Group stated that it was important for any licence condition to dovetail with the requirements of GS(M)R and safety cases, and that they furthermore would not support any move away from the current single gas emergency number.
- 5.125. A DISG member, representing a shipper/supplier, asked whether Transco's practice of advertising 0800 numbers on its assets would be continued by new

³³ Other GTs (i.e. IGTs) will continue to have the same provisions operative through their Amended Standard Condition 6.

owners. In particular whether this information would be displayed on the vans of new owners. A potential purchaser indicated that they thought it was unlikely that any new owner would object to publishing the 0800 number. An IGT representative noted that IGTs under GS(M)R are required to put the 0800 number on certain assets.

- 5.126. A DISG member, representing a shipper/supplier, stated that the condition should be split between the different emergency services.

Ofgem's proposals

- 5.127. The wider issues associated with emergency service provision are set out in Chapter 4.
- 5.128. Ofgem agrees with the comments raised by respondents that a pre requisite of any DN Sales should be an integrated and consistent response to Emergency situations. The discussion of the treatment of emergency services both in this chapter and Chapter 4 is in order to ensure that this is the case. The outcome of these discussions will also ensure that there is a clear definition of the roles of different GTs in relation to emergencies at DN boundaries, on IGT networks and on the NTS. Ofgem also agrees that the obligations in the licences relating to emergency services are consistent with requirements of GTs' safety cases and GS(M)R.
- 5.129. Ofgem has considered issues relating to the scope of obligations relating to emergency services in Chapter 4. In light of the proposals set out in that chapter we do not consider it necessary at this stage to increase the scope of Amended Standard Condition 6 but instead, where necessary, to introduce new licence conditions where appropriate (for example, relating to the provision of emergency services in respect of the NTS).
- 5.130. In respect of the comments raised in relation to the 0800 telephone number. Ofgem considers that, consistent with the current arrangements regarding IGTs, the provisions of this condition allow GTs, other than Transco, to discharge their obligations to provide a telephone service contractually via Transco.
- 5.131. Ofgem understands that requirements relating to the advertisement of the 0800 number are generally contained within the safety regulation. Ofgem therefore

does not consider it appropriate to duplicate such requirements within the licences of DN and NTS GTs. Ofgem welcomes the views of respondents on this issue.

- 5.132. Ofgem therefore continues to believe it to be appropriate for the provisions contained in this condition to be placed in the licences of all NTS and DN owners as Standard Special Condition A8. The amended standard condition will revert to the designated standard condition within the licences of all DN and NTS GTs. The condition will then be switched off in all such licences.
- 5.133. Finally, given the Authority's decision on legal separation, it may be necessary to make a minor amendment to paragraph 4 of Standard Special Condition A8 to ensure that the requirement for no undue discrimination apply applies between business units of a single company.³⁴ Ofgem intends to discuss this matter further at an upcoming DISG meeting.
- 5.134. The drafting for this Condition (Standard Special Condition A8) is provided for comment in Appendix 7B.
- 5.135. Ofgem invites respondents' views on its proposals for Amended Standard Condition 6. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be consulted upon in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 7 – Provision of Information Relating to Gas Illegally Taken

Description

- 5.136. This condition allows for the investigation and recovery of the value of gas illegally taken as well as the amendment of shipper charges and payment of

³⁴ This amendment would be similar to the one proposed in relation to Amended Standard Condition 4E (or Standard Special Condition A6).

allowances to suppliers to account for the costs incurred during this process subject to the provisions of Schedule 2B of the Gas Act.

- 5.137. The licensee is also required to restore the safety of meters or installations at the request of the relevant shipper, where the meter or installation is unsafe as the result of an offence or an attempted offence.

September document

- 5.138. As part of the informal licence consultation, Ofgem detailed that it was minded not to propose any modifications to this condition and therefore that Standard Condition 7 would continue to apply to all GT licences.

Respondents' views

- 5.139. Ofgem did not receive any comments in relation to this proposal.

Ofgem's views

- 5.140. Ofgem continues to consider it appropriate for Standard Condition 7 to apply to all GT licence holders.
- 5.141. The wording of this Condition (Standard Condition 7) is provided in Appendix 7A.
- 5.142. Ofgem invites respondents' views on its proposals for Standard Condition 7. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be consulted upon in February 2005. Further consultation may take place during this period through the DISG meetings.

Amended Standard Condition 8 – Provision and Return of meters

- 5.143. Amended Standard Condition 8 places a requirement on Transco to comply with any reasonable request received from a relevant supplier to provide, through a Meter Asset Manager, and install at the premises of a domestic customer a gas meter owned by Transco which is of a type specified by the supplier.

September document

- 5.144. In the informal licence consultation Ofgem considered that Amended Standard Condition 8 should reside within the NTS and DN-GT licences as a standard special condition. Ofgem perceived that this would ensure that the relevant GT would be required to comply with any request received from a supplier in relation to the provision of a meter. In meeting this obligation, the GT would be required to contract with Transco for metering services, or an alternative metering services provider, for the provision of these services to customers on its network.

Respondents' views

- 5.145. Ofgem received four responses concerning Amended Standard Condition 8.
- 5.146. A potential purchaser, did not consider it to be appropriate for the 'meter provider of last resort' to apply equally to DNs retained by Transco and IDNs. This potential purchaser suggested that these provisions should apply in a Special Condition applying only to Transco's RDNs.
- 5.147. A shipper/supplier detailed that, in relation to the provision of metering services, that Transco should be required to re-write its RGMA contracts, legacy contracts and the Meter Asset Managers Code of Practice in order to ensure that obligations incorporated within these documents are effectively retained.
- 5.148. A shipper/supplier suggested that if DNs were to obtain metering assets in compliance with the metering supplier of last resort obligations safeguards should be put in place, under Amended Standard Condition 29, to require DNs to obtain Ofgem's permission prior to the disposal of metering assets.
- 5.149. A further shipper/supplier response outlined its views that this obligation combined with those under Standard Condition 14 should result in any new metering services provider meter asset management manual being compliant with the RGMA baseline to avoid significant costs being imposed on suppliers.

Ofgem's proposals

- 5.150. Ofgem continues to believe that it is appropriate to introduce a standard special condition for NTS and DN licensees to replicate the provisions in Amended

Standard Condition 8. The drafting for this Condition (Standard Special Condition A10) is provided for comment in Appendix 7B.

- 5.151. In response to the respondent who stated that the provisions should only apply to the NTS and RDN licensees, Ofgem can see no justification to impose different metering obligations on RDNs from IDNs. Throughout the DN Sales process Ofgem has been clear that these 'metering of last resort' obligations would reside with the relevant network operator regardless of ownership. Ofgem continues to consider that IDNs can meet this obligation by contracting with Transco Metering Services or an alternative metering services provider for the provision of these services to customers on its network.
- 5.152. Ofgem invites respondents' views on its proposals for Amended Standard Condition 8. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Amended Standard Condition 9 – Network Code

Description

- 5.153. This condition obliges the licensee to establish a Network Code to facilitate the achievement of one of a number of specified code objectives including, amongst other things, the efficient and economic operation of its pipeline system and the efficient discharge of its obligations under its GT licence.
- 5.154. Amended Standard Condition 9 also requires the licensee to establish Code modification rules which set out the procedures for reviewing the Network Code and the conduct of proposals. The Authority's approval is required to modify the Network Code and the Authority retains the power to direct modifications to the Network Code without consultation. Changes to Code modification rules may only take place with the consent of the Authority following consultation with relevant shippers.

September document

- 5.155. Ofgem detailed as part of its informal licence consultation that Amended Standard Condition 9 would need to be substantially revised to support the final form of the proposed commercial arrangements.
- 5.156. In the consultation Ofgem invited respondents' views regarding:
- ◆ Transco's proposal that the Network Code should be modified to create a UNC with short form codes (SFCs) for each gas transporter that becomes a signatory to the UNC;
 - ◆ the conclusion of the Authority and the workgroups that agency arrangements and the JO would be necessary in a divested industry structure to prevent any undue discrimination on the behalf of Transco in the running of the modification process;
 - ◆ the conclusion of the workgroups that in view of the introduction of the agency and JO it would be necessary to introduce a new UNC objective;
 - ◆ the inclusion of the code modification rules in the UNC, as well as the scope of the functions of the Agency;
 - ◆ the suitability of retaining provisions which require that a UNC can only be modified following the receipt of consent from the Authority; and
 - ◆ appropriate governance arrangements for offtakes from the NTS.

- 5.157. As part of the licence consultation, Ofgem detailed that it was intending to introduce any new provisions as standard special conditions in the NTS and DN-GT licences.

Respondents' views

- 5.158. Ofgem received 6 responses concerning Amended Standard Condition 9. This condition has also been the subject of a number of discussions through DISG.
- 5.159. The respondents' views relating to whether there should be a separate Offtake Code and the role of the Joint Office within the Network Code process are set

out in detail in Chapter 4. In addition the following points have been expressed by respondents:

- ◆ one shipper/supplier stated that it considered this condition needed to change but it was unsure as yet of the scope of the changes. This shipper/supplier saw no need to amend the consent to modify provisions. This view was supported by a potential purchaser;
- ◆ one shipper/supplier and one potential purchaser supported the introduction of a new relevant objective to ensure the efficient administration and implementation of the arrangements (to include the Joint Office and the Agency). This shipper/supplier also considered that it was an essential safeguard to include the scope of the agency in the UNC although, in contrast, one potential purchaser did not consider that this would be necessary;
- ◆ NGT supported the UNC and SFC proposal. NGT did not see the need for an efficient administration relevant objective but did see the need for such a requirement. NGT also stated that the licence condition should be revised to reflect that the modification rules which will be set out in the UNC; and
- ◆ one potential purchaser considered that modification rules associated with the UNC should be included within the UNC.

5.160. DISG members also considered this condition. One DISG member, representing a shipper/supplier, stated that it was important for the condition to oblige the NTS and DN-GTs to enter into Agency Arrangements. A further DISG member raised the issue of whether IGTs should also be covered by the proposals. A potential purchaser considered that it was important for the Authority to retain its powers to 'consent to modify' at least until after DN Sales was complete.

5.161. A further DISG member, representing a shipper/supplier stated that they were concerned that the condition did not adequately reflect the role of the Joint Office. This representative was also concerned that the Short Form Codes could become very substantial. They additionally considered that the condition should be expanded to cover transitional arrangements. The same DISG member stated that it was important for all the UNC modification procedures to be set out in the

UNC. They also suggested a requirement should be introduced for Ofgem to carry out a cost benefit analysis on all major modification proposals.

Ofgem's proposals

- 5.162. As set out in Chapter 4 Ofgem considers that it is appropriate for the offtake arrangements to be set out within the UNC and therefore that there will be no separate Offtake Code. In addition Ofgem considers that the Joint Office should have responsibility for the administration of the UNC modification procedures.
- 5.163. In response to the views expressed by those respondents who commented on the issue, Ofgem considers it appropriate to retain the provisions allowing consent to modify the Network Code.
- 5.164. In respect of the proposed relevant objective regarding the efficient administration and implementation of arrangements, Ofgem continues to consider that this objective is necessary despite the views of NGT. Ofgem considers that it is important to be able to look at modification proposals against this objective particularly as regards the provisions of the Network Code which relate to the Joint Office and Agency.
- 5.165. In respect of the comment raised by a respondent that there needs to be an obligation on NTS and DN-GTs to be party to the Agency arrangements, Ofgem considers that this should be imposed through a new licence condition on Agency Arrangements (Standard Special Condition A15) which is discussed in Chapter 6 of this document.
- 5.166. We consider that the Relevant Objectives of the Network Code as set out in Standard Special Condition A11 are sufficient criteria for Ofgem to consider when deciding whether to direct a modification and involve an assessment of the advantages and disadvantages of any modification proposals.
- 5.167. Ofgem agrees with the respondents and DISG participants who stated that the modification rules of the UNC should sit within the UNC itself.
- 5.168. Ofgem notes the view of one respondent regarding cost benefit analysis for major modification proposals. However, it should also be recognised that the Authority has obligations under section 5A of the Utilities Act to carry out impact assessments with respect to Network Code proposals that the Authority

considers to be important within the meaning of section 5A(2) of the Utilities Act.

- 5.169. In respect to the point raised at DISG regarding transitional arrangements, Ofgem does not consider it necessary at this stage to expand this condition to cover transitional arrangements. These issues are being progressed through Transco's UNC development forum.
- 5.170. Ofgem has drafted a standard special condition for NTS and DN GTs to replace Amended Standard Condition 9. Standard Special Condition A11 is substantially different from the current Amended Standard Condition 9 (which will be switched off), to reflect the new governance and industry code arrangements that have been discussed substantially through the workgroup process and in the informal licence consultation. The key changes are as follows:
- ◆ the introduction of a new relevant objective: to ensure the co-ordinated, efficient and economical development of pipeline systems so far as it is consistent with the efficient and economic development of the licensee's pipeline system. We do not at this time consider it appropriate to introduce this Relevant Objective into the licences of IGTs as this is not central to the DN Sales process;
 - ◆ the introduction of a second new relevant objective relating to the promotion of efficiency in the implementation and administration of the Network Code. This provision is designed to govern both the Agency and the Joint Office arrangements. These provisions are set out in paragraph 1 of Standard Special Condition A11; and
 - ◆ requirements on licensees to create and be party to a UNC with short form codes (SFCs) for each gas transporter that becomes a signatory to the UNC.
- 5.171. The drafting for this Condition (Standard Special Condition A11) is provided for comment in Appendix 7B.
- 5.172. In addition to the requirements set out in Standard Special Condition A11, three new conditions are required to augment these provisions. These relate to the requirements for Independence of the Balancing Arrangements (Standard Special

Condition A16 and NTS Special Condition C6) and LNG related provisions (NTS Special Condition C1).

5.173. As discussed in Chapter 4, to address the issue of LNG:

- ◆ this standard special condition has reverted to the references to LNG storage facilities contained in the standard conditions designated by the Secretary of State under the Utilities Act; and
- ◆ a new NTS Special Condition has been introduced to “augment” this standard special condition with LNG related provisions (Special Condition C1, paragraph 6). This is discussed in further detail in Chapter 6.

5.174. Ofgem is also intending to introduce new requirements associated with both the Joint Office, the Common Systems Arrangements and the Agency arrangements (Standard Special Condition A12, A14 and A15 respectively). These are discussed in Chapter 6.

5.175. Ofgem invites respondents’ views on its proposals for Amended Standard Condition 9. Following consideration of respondents’ views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 13 – Change co-ordination for the Utilities Act 2000

Description

5.176. This condition requires the licensee to take all reasonable measures to secure and implement specified industry framework documents necessary to give full effect to the Utilities Act 2000. This condition is now time expired.

September document

5.177. As part of the informal licence consultation Ofgem proposed to retain this condition within the licences of the NTS and DN GT licensees but to switch the condition off. Ofgem detailed that it may propose, at some point in the future (outside of the DN sales process), to remove this condition from all GT licences.

Respondents' views

5.178. Ofgem did not receive any comments in relation to this proposal.

Ofgem's proposals

5.179. Ofgem acknowledges that its proposals for Standard Condition 13 do not directly relate to DN Sales. However, Ofgem continues to believe that it is desirable as part of this process to switch off time expired conditions to give clarity to licensees (particularly any new purchasers of DNs) as to the obligations within their licence. Ofgem therefore will switch off this condition and switch this condition off in the licences of other GTs at a suitable opportunity.

5.180. Ofgem invites respondents' views on its proposals for Standard Condition 13. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be consulted upon in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 14 – The Supply Point Administration Agreement

Description

5.181. Standard Condition 14 was recently introduced and requires the licensee to be a party to and comply with the relevant provisions of the Supply Point Administration Agreement (SPAA).

September document

5.182. In the informal licence consultation Ofgem stated that it was minded not to propose any modifications to this condition and, as such, Standard Condition 14 would continue to apply to all GT licences including NTS and DN-GTs.

Respondents' views

5.183. Ofgem did not receive any comments in relation to this proposal.

Ofgem's proposals

5.184. Ofgem continues to propose that Standard Condition 14 will continue to apply to all GT licences including NTS and DN-GTs.

5.185. The wording of this Condition (Standard Condition 14) is provided in Appendix 7A.

5.186. Ofgem invites respondents' views on its proposals for Standard Condition 14. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 16 – Pipeline System Security Standards

Description

5.187. This condition is one of a number regulating security of supply. Under Standard Condition 16 the licensee is required to plan and develop its pipeline system to enable it to meet the peak daily demand for gas such that the ability of the pipeline system to meet that demand is only expected to be exceeded in 1 year out of 20 based on the previous 50 years of data (the 1 in 20 obligation).

September document

- 5.188. In the context of the offtake arrangements RIA³⁵, Ofgem considered whether, in the event of DN Sales proceeding, the 1 in 20 obligation should be removed. The Authority reached the decision that such an amendment would not be appropriate at this time but that further consideration of the implications of the removal of the 1 in 20 obligation would be necessary outside of DN Sales.
- 5.189. Therefore, as part of the informal licence condition Ofgem was minded not to propose any modifications to this condition and, as a result, Standard Condition 16 would continue to apply to all GT licences including NTS and DN-GTs.

Respondents' views

- 5.190. Eleven respondents provided comments in relation to the 1 in 20 obligation and all of these respondents expressed support for the proposal to retain this condition.
- 5.191. Two shipper/suppliers outlined their support for Ofgem's proposal. One shipper/supplier raised in its response that a requirement should be put on DN-GTs to ensure a common methodology is used for the calculation of the 1 in 20 requirement. One shipper/supplier raised a concern as to whether short term allocations which required NTS connectees (other than DNs) to compete with DNs for a finite amount of capacity would be inconsistent with the 1 in 20 obligation. A potential purchaser also stated its view that it was important to ensure that the offtake arrangements do not jeopardise the 1 in 20 requirements. NGT stated that the licence obligations should remain in place to ensure a consistent security standard. NGT considered that clarity of the role of transmission was important. NGT stated that if the 1 in 20 obligation is to remain in the NTS licence then it is important that the obligation should be aligned with either the current licence or the Network Code. NGT also stated that this should be checked for consistency with the gas security of supply directive.

³⁵ *National Grid Transco – Potential sale of gas distribution network businesses, Offtake Arrangements Regulatory Impact Assessment*, Ofgem, June 2004.

Ofgem's proposals

- 5.192. As set out in Chapter 4 it may be necessary to modify Standard Condition 16 to reflect Transco's proposals for the flexibility product. In any such modification, Ofgem would seek to ensure that the revised condition has the same effect as it currently has under Transco's common ownership. As these issues are still in consideration in Transco's exit development forum Ofgem will not be proposing any modifications or providing any drafting relating to Standard Condition 16 as part of this document. It is therefore proposed at this stage that Standard Condition 16 will apply to all GTs including NTS and DN licensees. However, if Ofgem considers later in the process that such modifications are required these will be informally consulted upon through the DISG.
- 5.193. The wording of this Condition (Standard Condition 16) is provided in Appendix 7A.
- 5.194. In relation to the concern expressed regarding short term allocations of capacity and interactions with the 1 in 20 obligation, Ofgem notes that the arrangements have been specifically designed to ensure that DNs can procure capacity on a long term basis and, therefore, meet its 1 in 20 obligation, irrespective of the arrangements for the allocation of capacity in the short term.
- 5.195. Ofgem invites respondents' views on its proposals for Standard Condition 16. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

**Amended Standard Condition 17 – Provision of Services for Persons
who are of Pensionable Age or Disabled or Chronically Sick:
Arrangements with respect to Meters**

Description

- 5.196. Amended Standard Condition 17 requires that Transco must comply with any request received from a gas supplier in relation to the repositioning of meters that it owns for customers who are of pensionable age, disabled or chronically sick. This is provided that the relevant supplier pays Transco's reasonable expenses in doing so. This condition was amended in Transco plc's GT licence as part of the Revised Gas Metering Arrangements (RGMA) changes introduced in July 2004.

September document

- 5.197. As part of the informal licence consultation Ofgem was of the opinion that, as DN-GTs would be required to provide metering services of last resort under the conditions contained within Amended Standard Condition 8, they should have an obligation of this nature within their licences. Ofgem was also mindful that the NTS-GT licence holder would continue to have permission under the Gas Act to convey gas to all premises including domestic premises. Ofgem therefore proposed to include this as a standard special condition applicable to both NTS and DN-GT licences.

Respondents' views

- 5.198. Two respondents expressed views in relation to this proposal.
- 5.199. One potential purchaser considered that NGT should retain responsibility for the metering obligation of last resort and that, as such, this condition should only apply to NGT.
- 5.200. NGT was of the opinion that the condition should be amended such that it would only apply to transporters supplying more than one domestic customer.

Ofgem's proposals

- 5.201. Following consideration of respondents' views on this issue Ofgem continues to consider it appropriate for this licence condition to apply to all NTS and DN-GT licensees. Ofgem does not see any justification for introducing different provisions for RDN and IDN-GT licensees and therefore does not consider that the metering of last resort obligations should apply only to Transco's RDNs.
- 5.202. Ofgem does not consider that it is necessary to amend this condition to state that the obligation only applies in respect of GTs who have one or more domestic customer connected to their network, as it is already drafted such that it only requires action in respect of domestic customers. Ofgem therefore proposes that the current provisions of Amended Standard Condition 17 will be introduced as a standard special condition in the licences of all NTS and DN-GTs. The drafting for this Condition (Standard Special Condition A19) is provided for comment in Appendix 7B.
- 5.203. The amended standard condition will therefore revert to the Designated Standard Condition in the licences of all NTS and DN-GTs, which will then be switched off.
- 5.204. Ofgem invites respondents' views on its proposals for Amended Standard Condition 17. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 18 – Provision of Services for Persons who are Blind or Deaf

Description

- 5.205. This condition requires licensees to prepare and submit to the Authority for approval a code of practice detailing the special services that will be made

available for domestic customers who are disabled by virtue of being blind or partially sighted, or deaf or hearing impaired.

September document

- 5.206. In the informal licence consultation Ofgem detailed that the NTS GT licence holder would continue to have permission under the Gas Act to supply gas to domestic premises and, as such, it considered that the condition should apply both to the NTS and DN-GT licences.
- 5.207. The condition currently obliges the licensee to have a code in place by 1 November 2001. Ofgem proposed to remove this time redundant wording and replace it with a new date in order that the new GT licensees would not automatically be in breach of the licence. The condition would then become a standard special condition in the licences of all NTS and DN-GTs.

Respondents' views

- 5.208. NGT stated that this condition should be amended to apply only when a GT has more than one domestic customer.
- 5.209. One potential purchaser agreed with Ofgem that, to avoid non-compliance, the time redundant wording should be removed but considered that the condition should continue to be subject to modification through the statutory CLM.

Ofgem's proposals

- 5.210. Ofgem considers it appropriate for this condition to be drafted such that it only applies to GT licensees when they have one or more domestic customers connected to their networks as this will avoid an obligation to produce a code which is redundant by virtue of there being no domestic customers connected to the network.
- 5.211. In order to avoid an automatic breach of this obligation by new licensees, Ofgem also proposes to amend this Condition such that the Authority may approve a date later than 1 November 2001.
- 5.212. Ofgem therefore proposes that the provisions currently set out in the standard condition will be amended in line with these proposals and placed in a standard

special condition that will apply to all NTS and DN-GTs. The drafting for this Condition (Standard Special Condition A20) is provided for comment in Appendix 7B.

5.213. The associated Designated Standard Condition will then be switched off in these licences.

5.214. Ofgem invites respondents' views on its proposals for Standard Condition 18. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 19 – Arrangements in Respect of Powers of Entry

Description

5.215. Standard Condition 19 requires the licence holder to prepare and submit a statement to the Authority regarding its proposed arrangements in respect of the steps to be taken under Standard Condition 19A (Authorisation of Officers).

September document

5.216. In the informal licence consultation Ofgem detailed that as this licence condition relates to both domestic and non-domestic premises it considered that it would be appropriate for this condition to apply to both the NTS and DN-GT licences. Ofgem was therefore minded not to propose any modifications to this condition other than to amend a cross reference to Standard Condition 22 as it is proposed that this will become a standard special condition as a result of the changes to that Condition.

Respondents' views

5.217. NGT stated that this condition should be amended to apply only when a GT has more than one domestic customer.

Ofgem's proposals

- 5.218. As this condition applies in respect of domestic and non-domestic customers Ofgem does not consider it appropriate to modify the condition in line with NGT's suggestion.
- 5.219. Ofgem therefore continues to consider it appropriate for this condition to apply to all NTS and DN GTs. In view of the need to amend the cross reference within the condition it will be necessary for the provisions contained in Standard Condition 19 to become a standard special condition applicable to DN and NTS GTs. The drafting for this Condition (Standard Special Condition A22) is provided for comment in Appendix 7B.
- 5.220. The Designated Standard Condition will then be switched off in all DN and NTS licences.
- 5.221. Ofgem invites respondents' views on its proposals for Standard Condition 19. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 19A – Authorisation of Officers

Description

- 5.222. This condition describes the requirements for officers to be appropriately qualified, identifiable by the public and to ensure that their equipment/identification is not misused. It also obliges licensees to inform relevant shippers, naming the agent in question.

September document

- 5.223. In the informal licence consultation Ofgem detailed that as this licence condition relates to both domestic and non-domestic premises it considered that it would

be appropriate for this condition to apply to both NTS and DN-GTs. Ofgem was therefore minded not to propose any modifications to this condition.

Respondents' views

- 5.224. NGT stated that this condition should be amended to apply only when a GT has more than one domestic customer.

Ofgem's proposals

- 5.225. As this condition applies to both domestic and non-domestic premises Ofgem cannot see any justification for wording the condition such that it would only apply to transporters that supply more than one domestic customer.
- 5.226. Ofgem therefore continues to consider it appropriate for the current Standard Condition (Standard Condition 19A) to remain unchanged, and therefore continue to apply to all GT licensees including all NTS and DN-GTs. The wording of this Condition is provided in Appendix 7A.
- 5.227. Ofgem invites respondents' views on its proposals for Standard Condition 19A. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 19B – Exercise of Powers of Entry

Description

- 5.228. Standard Condition 19B requires the licensee to use reasonable endeavours to avoid undue disturbance to owners or occupiers of premises as a result of the exercise of the powers of entry conferred by Schedule 2B of the Gas Act.

September document

5.229. In the informal licence consultation Ofgem detailed that as this licence condition relates to both domestic and non-domestic premises it considered that it would be appropriate for this condition to apply to both NTS and DN-GTs. Ofgem was therefore minded not to propose any modifications to this condition.

Respondents' views

5.230. NGT stated that this condition should be amended to only apply when a GT has more than one domestic customer.

Ofgem's proposals

5.231. As this condition applies to both domestic and non-domestic premises Ofgem cannot see any justification for wording the condition such that it would only apply to transporters that supply one or more domestic customer.

5.232. Ofgem therefore continues to consider it appropriate for the current standard condition (Standard Condition 19B) to remain unchanged, and therefore continue to apply to all GT licensees including all NTS and DN-GTs. The wording of this Condition is provided in Appendix 7A.

5.233. Ofgem invites respondents' views on its proposals for Standard Condition 19B. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Amended Standard Condition 20 – Standards of Performance

Description

5.234. This condition describes the conditions of payment of compensation to consumers under Section 33AA of the Gas Act.

September document

- 5.235. As part of the informal licence consultation Ofgem was minded not to propose any modifications to this condition and, as such, Standard Condition 20 would continue to apply to all GT licences including NTS and DN-GTs.

Respondents' views

- 5.236. NGT stated that this condition should be amended to only apply when a GT has more than one domestic customer.

Ofgem's proposals

- 5.237. As this condition applies to both domestic and non-domestic premises Ofgem does not consider it to be appropriate to word the condition such that it would only apply to transporters that supply more than one domestic customer.
- 5.238. Ofgem therefore continues to consider it appropriate for the current standard condition (Standard Condition 20) to remain unchanged, and therefore continue to apply to all GT licensees including all NTS and DN-GTs. The wording of this Condition is provided in Appendix 7A.
- 5.239. Ofgem invites respondents' views on its proposals for Amended Standard Condition 20. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 21– Complaint Handling Procedure

Description

- 5.240. This condition requires the licensee to put in place a code of practice by 1 November 2001 detailing the procedure for handling complaints from domestic customers about the manner in which the licensee conducts its transportation business.

September document

- 5.241. In the informal licence consultation Ofgem detailed that the NTS GT licence holder would continue to have permission under the Gas Act to supply gas to domestic premises and, as such, it considered that the condition should apply both to the NTS and DN-GT licences.
- 5.242. As set out above there is an obligation to have a code in place by 1 November 2001. Ofgem proposed the removal of this time redundant wording and replacing it with a new date in order that the DNs would not automatically be in breach of the licence. As such, Ofgem proposed that this Condition should become a standard special condition applicable to all NTS and DN-GTs.

Respondents' views

- 5.243. NGT stated that this condition should be amended to only apply when a GT has more than one domestic customer.
- 5.244. One potential purchaser agreed with Ofgem that, to avoid non-compliance, the time redundant wording should be removed but considered that the condition should continue to be subject to modification through the statutory CLM.

Ofgem's proposals

- 5.245. Following consideration of respondents' views, Ofgem considers it to be appropriate for this condition to be drafted such that it only applies to NTS and DN-GT licensees when they have one or more domestic customers connected to their networks as this will avoid an obligation to produce a code of practice which is redundant by virtue of there being no domestic customers connected to the network.
- 5.246. In order to avoid an automatic breach of this obligation by new licensees, Ofgem proposes to amend this Condition such that the Authority may approve a date later than 1 November 2001.
- 5.247. Furthermore, given the proposed amendments to Standard Condition 22, it has been necessary to amend the cross-references to this condition in paragraph 3.

- 5.248. Ofgem therefore proposes that the provisions currently set out in the standard condition will be amended in line with these proposals and placed in a standard special condition that will apply to all NTS and DN-GTs. The drafting for this Condition (Standard Special Condition A23) is provided for comment in Appendix 7B.
- 5.249. The associated Designated Standard Condition will then be switched off in these licences.
- 5.250. Ofgem invites respondents' views on its proposals for Standard Condition 21. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 22 – Preparation, Review of and Compliance with Statements and Codes

Description

- 5.251. Standard Condition 22 details licensee obligations with respect to the statements and codes required pursuant to Standard Conditions 18, 19 and 21, such as the need to consult the Consumer Council and the obligation to review such statements whenever requested by the Authority.

September document

- 5.252. In the informal licence consultation Ofgem detailed that it was minded not to propose any modifications to this condition other than to make cross reference changes to reflect the proposed changes to Standard Conditions 18 and 21.

Respondents' views

- 5.253. NGT stated that this condition should be amended to apply only when a GT has more than one domestic customer.

- 5.254. DISG members considered this condition. One potential purchaser was of the opinion that the prospective buyers of DNs would need time to consider the statements and codes incorporated under Standard Condition 22.

Ofgem's proposals

- 5.255. Ofgem considers that this condition should apply to the licences of all NTS and DN-GTs as some of its provisions relate to codes which all NTS and DN-GT licence holders will have in place regardless of whether they supply domestic customers or not.
- 5.256. Ofgem notes the concern, of the potential purchaser, surrounding compliance. Ofgem understands that NGT is planning to put relevant statements in place. Potential purchasers could then modify these statements as they see fit.
- 5.257. The condition will therefore only change as necessary to refer to the new numbering of current Standard Conditions 18, and 21. Given these cross-referencing amendments, the provisions will be placed within a standard special condition in the licences of NTS and DN-GTs. The drafting for this Condition (Standard Special Condition A24) is provided for comment in Appendix 7B.
- 5.258. The associated Designated Standard Condition will then be switched off in these licences.
- 5.259. Ofgem invites respondents' views on its proposals for Standard Condition 22. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 23 – Record of and Report on Performance

Description

- 5.260. This condition requires the licensee to keep a record of performance in relation to the general operation of the arrangements referred to in Standard Conditions

18 to 22 and the provision of services to domestic customers. The licensee must publish and provide an annual report on this to the Authority and the Consumer Council.

September document

- 5.261. Ofgem detailed, in the informal licence consultation that it was minded not to propose any modifications to this condition other than to change references to other conditions as with Standard Condition 22.

Respondents' views

- 5.262. NGT stated that this condition should be amended to only apply when a GT has more than one domestic customer.

Ofgem's proposals

- 5.263. As this condition contains provisions which relate to both domestic and non-domestic customers, Ofgem considers it to be appropriate for the condition to apply to all NTS and DN-GTs.
- 5.264. Therefore the only modification to this condition will be to change the cross references to the other conditions as with Standard Condition 22. The provisions contained within this condition, with cross referencing changes, will form a standard special condition in the licences of NTS and DN-GTs. The drafting for this Condition (Standard Special Condition A25) is provided for comment in Appendix 7B.
- 5.265. The associated Designated Standard Condition will then be switched off in these licences.
- 5.266. Ofgem invites respondents' views on its proposals for Standard Condition 23. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Amended Standard Condition 24 – The Provision of Information to the Authority

Description

- 5.267. This condition requires that information and reports that the Authority may reasonably require or which may be necessary for it to perform its functions, are provided to the Authority on request. The licensee cannot be required to produce any documents or give any information which it could not be compelled to produce or give in evidence in civil proceedings before a court.

September document

- 5.268. In the informal licence consultation Ofgem detailed that this condition would need to be amended to reflect the businesses which each of the NTS-GT and DN-GT licensees will conduct and in particular as to how LNG Storage and metering services were being treated within the licence.

Respondents' views

- 5.269. One potential purchaser provided a response to this proposal and considered that the NTS GT licence should be amended to include LNG storage. This respondent held the view that RDNs should assume responsibility for the provision of metering services of last resort as Transco has not contracted with the IDNs to sell its metering assets and, consistent with this, considered that only the RDN licence should be amended to include a reference to metering.
- 5.270. DISG members have considered this condition. One shipper/supplier held the view that this condition was central to ensuring that customers achieve benefits from comparative regulation.

Ofgem's proposals

- 5.271. Following Ofgem's decisions relating to LNG Storage and metering services and meter reading services, Ofgem proposes that the provisions in this condition should apply to all NTS and DN-GTs, except insofar as they relate to LNG Storage. The LNG Storage provisions should apply only to the NTS-GT. As discussed in Chapter 4, Ofgem considers that the metering services and meter

reading provisions should apply to all NTS and DN-GTs and that there is no justification for treating IDN and RDNs differently in respect of such obligations.

5.272. In order to incorporate the changes made to the Designated Standard Condition contained in the amended standard condition in Transco plc's licence which refer to metering services and meter reading services the provisions in this condition will be set out in a standard special condition in the licences of all NTS and DN-GTs. The drafting for this Condition (Standard Special Condition A26) is provided for comment in Appendix 7B.

5.273. As discussed in Chapter 4, to address the issue of LNG:

- ◆ this standard special condition has reverted to the references to storage facilities contained in the standard conditions designated by the Secretary of State under the Utilities Act; and
- ◆ a new NTS Special Condition has been introduced to "augment" this standard special condition with LNG related provisions (Special Condition C1, paragraph 7). This is discussed in further detail in Chapter 6.

5.274. The amended standard condition will then revert to the Designated Standard Condition in the licences of all NTS and DN-GTs, which will then be switched off.

5.275. Ofgem invites respondents' views on its proposals for Amended Standard Condition 24. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Amended Standard Condition 25 – Long Term Development Statement

Description

- 5.276. Amended Standard Condition 25 is a system planning condition obliging the licensee to produce, and update annually, a statement of the forecast use and development of the high pressure system for the next 10 years. The licensee is obliged to submit a copy of the statement and any revisions to the Authority.

September document

- 5.277. In the informal licence consultation Ofgem proposed that consideration should be given as to whether this obligation should be placed upon NTS and DN GT licensees in respect of their networks. As such the NTS and DN GTs would be required to produce statements in relation to their respective networks.
- 5.278. Transco's alternative proposal required a single co-ordinated 10-year statement to be prepared, covering the whole of Great Britain. Ofgem considered this proposal to be inappropriate given its views on the necessary separation requirements that would be required between the NTS and Transco's RDNs.
- 5.279. Ofgem proposed the introduction of a new standard special condition to deal with the matters in this condition.

Respondents' views

- 5.280. Five respondents submitted comments regarding this condition. One potential purchaser considered that it would be important for DN to produce a ten year statement as well as the NTS and emphasised the importance of information sharing between the NTS and DN following a potential DN sale. The respondent also perceived that it may be difficult for the NTS and DN-GTs to produce a consolidated document if the issue of discrimination were to remain a concern. In contrast, a second potential purchaser supported compilation of a single coordinated statement and considered that licence conditions should be placed respectively on the NTS and DN GTs to produce the statement and to coordinate with the NTS for the production of a joint statement.
- 5.281. Three respondents, representing shippers, supported Transco's proposals and considered that the NTS should be responsible for the compilation of a

coordinated ten year statement with associated input from DNs. Of these, one was of the opinion that benefits could be achieved by requiring the NTS and the DN-GTs to provide a consolidated long term development statement. Another considered that the production of a coordinated statement would continue to provide a useful coordinated view on the GB gas supply-demand balance and the need for development of the high pressure system.

- 5.282. This condition has also been considered by DISG participants. One shipper/supplier considered that there would be an interaction between the offtake arrangements and the ten year statement while a second was of the opinion that it would be important for the industry to be able to see NTS and DN-GTs' networks as one system developed on an integrated basis. A potential purchaser also stated that although it understood Ofgem's concerns regarding information sharing between the NTS and DNs, some co-ordination of the ten year statement would be appropriate.

Ofgem's proposals

- 5.283. Following consideration of respondents' views, Ofgem considers it to be appropriate for the DN licensees and the NTS licensee to be obliged to compile and produce a 10 year statement for their own networks following a direction from the Authority. Ofgem also agrees with respondents that it would be important for the NTS to use information from the DNs when compiling its report.
- 5.284. Ofgem proposes that the DN-GTs should be obliged to furnish other GTs with a copy of their statement if directed to do so by the Authority. The NTS-GT will then be obliged to include information relating to its pipeline system and any other pipeline system if directed by the Authority. This will then allow the NTS (if such directions are made) to use the information contained in the DNs' reports when drafting its report.
- 5.285. Ofgem therefore proposes that a standard special condition should be introduced in the licences of all DN-GTs and a Special Condition should be introduced in the licences of Transco's NTS-GT containing these provisions as amended in line with Ofgem's proposals. The proposed drafting for these

conditions (Standard Special Condition D3 and Special Condition C2) is provided in Appendix 7B.

- 5.286. Amended Standard Condition 25 will then revert to the Designated Standard Condition in the licences of all NTS and DN-GTs, which will then be switched off.
- 5.287. Ofgem invites respondents' views on its proposals for Amended Standard Condition 25. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 27 – Adjustments of Amounts by Reference to the Retail Price Index

Description

- 5.288. Where a standard condition provides for an amount to be adjusted, this condition defines the appropriate adjustment mechanism using the retail price index (RPI).

September document

- 5.289. In the informal licence consultation Ofgem detailed that it was minded not to propose any modifications to this Condition so that Standard Condition 27 would continue to apply to all GT licences including NTS and DN-GTs.

Respondents' views

- 5.290. No respondents raised comments relating to this condition.

Ofgem's proposals

- 5.291. Following consideration of the respondents' views and the discussions at DISG, Ofgem continues to propose not to make any modifications to this standard

condition so that it continues to apply to all GT licences including NTS and DN-GTs. The wording of this Condition is provided in Appendix 7A.

- 5.292. Ofgem invites respondents' views on its proposals for Standard Condition 27. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 28 – Termination of Shipping Arrangements

Description

- 5.293. Standard Condition 28 requires the licence holder to keep relevant suppliers informed about the terms which are specified for the purposes of Standard Condition 24B of their gas suppliers' licences (Undertakings to be Given by Licensee to Relevant Transporters in Respect of Shipping Charges etc).

September document

- 5.294. As part of the informal licence consultation Ofgem stated that it was minded not to propose any modifications to this Condition so that Standard Condition 28 would continue to apply to all GT licences including NTS and DN-GTs.

Respondents' views

- 5.295. Ofgem did not receive any comments in relation to this proposal.

Ofgem's proposals

- 5.296. Ofgem continues to consider it to be appropriate not to make any modifications to this condition so that Standard Condition 28 will apply to all GT licensees including NTS and DN-GTs. The wording of this Condition is provided in Appendix 7A.

5.297. Ofgem invites respondents' views on its proposals for Standard Condition 28. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Amended Standard Condition 29 – Disposal of Assets

Description

- 5.298. This condition provides that the licensee must not dispose of, or relinquish operational control over, any transportation asset or LNG storage asset otherwise than in accordance with this Condition.
- 5.299. It sets out that a licence holder is required to give the Authority not less than two months' prior written notice of its intent to dispose of, or relinquish operational control over, any transportation asset or LNG storage asset together with any further information relating to the transaction that the Authority may request.
- 5.300. Where a transportation asset comprises a significant part of an independent system operated by the licensee, the licensee must, save where the Secretary of State consents otherwise, not dispose of the asset or its right to operate the asset until it has put in place or secured suitable alternative arrangements.
- 5.301. The licensee may dispose of or relinquish operational control over a transportation or LNG storage asset where the Authority has issued a direction containing a general consent to the transaction, disposal or relinquishment of a specified asset and the disposal is in accordance with any conditions to which the consent is subject or where the disposal is required by legislation.

September document

- 5.302. In the informal licence document, Ofgem considered that it would be important to retain the same degree of regulatory control over network owners and their disposal of assets or relinquishment of control over them after any DN sales.

5.303. Ofgem proposed that the new standard special condition in relation to the NTS and DN-GTs would be equivalent to the obligations upon electricity transmission and distribution companies in line with the decision in 2001 to allow the use of group service companies to provide asset management and potentially network control services where more than one licensed network is owned by the same group of companies.

Respondents' views

5.304. One potential purchaser commented that, in principle, it supported the proposal to include provisions similar to those in the electricity distribution licence. However, the respondent considered that under SOMSA arrangements Transco would be responsible for providing control centre activities to DNs for a transitional period and that this could be interpreted as relinquishing operational control of an asset when the transaction is completed.

Ofgem's proposals

5.305. Ofgem continues to consider that it is important to retain the same degree of regulatory control over network owners and their disposal of assets or relinquishment of control over them after any DN sales.

5.306. Ofgem is still considering the point raised by the respondent that the passing over of control centre activities to DNs by NGTs at the time at which the SOMSAs expire could be interpreted as relinquishing operational control of an asset when the transaction is completed. Ofgem will consult with the DISG on this issue, if necessary.

5.307. Ofgem therefore proposes that the provisions contained in this amended standard condition (which include changes from the Designated Standard Condition regarding the definition of "Relinquishment of Operational Control") will be placed in a standard special condition applicable to all NTS and DN GT licensees. The drafting for this Condition (Standard Special Condition A27) is provided for comment in Appendix 7B. However, further changes to this drafting is required to reflect Ofgem's proposals as set out above. This revised drafting will be issued to the DISG for consultation prior to the publication of the formal Section 8AA notice (and associated Section 23 notice).

5.308. As discussed in Chapter 4, to address the issue of LNG:

- ◆ this standard special condition has reverted to the references to LNG storage facilities contained in the standard conditions designated by the Secretary of State under the Utilities Act; and
- ◆ a new NTS Special Condition has been introduced to “augment” this standard special condition with LNG related provisions (Special Condition C1, paragraph 8). This is discussed in further detail in Chapter 6.

5.309. It should be noted that the provisions with respect to independent networks (and associated cross-references to what was formerly Special Condition 18) have been retained within this condition. However, the future treatment of Special Condition 18 is currently being considered by the DTI, and any consequential changes will be reflected within Standard Special Condition A27 as appropriate.

5.310. The amended standard condition will then revert to a Designated Standard Condition within all NTS and DN-GT licences, which will then be switched off.

5.311. Ofgem invites respondents’ views on its proposals for Amended Standard Condition 29. Following consideration of respondents’ views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Amended Standard Condition 30 – Regulatory Accounts

Description

5.312. Amended Standard Condition 30 sets out the obligations on the licence holder as regards its regulatory accounts. It includes the duty to produce separate annual regulated accounts in respect of each of its separate businesses and to provide copies of these to the Authority.

September document

- 5.313. Ofgem set out as part of its September document that it considered transparency, associated with the provision of regulatory accounts, to be critical in the completion of its analysis of the comparative performance of the DN businesses in the restructured industry post DN sales. As such, Ofgem proposed that where a licensee conducts more than one DN business this condition should ensure that information is provided separately in relation to each DN.
- 5.314. Furthermore, the informal licence consultation document stated that, as the Authority was minded to require separate licences for the NTS and Transco's RDNs, consideration would need to be given to which businesses were relevant to each licensee. The treatment of LNG storage is discussed in further detail in Chapter 4.
- 5.315. Ofgem proposed that the regulatory accounts provisions would take the form of a standard special condition applicable to NTS and DN-GTs and augmented, where appropriate, by Special Conditions.

Respondents' views

- 5.316. Three potential purchasers, two shippers and NGT provided a response in relation to this condition. All six of these respondents agreed with Ofgem's proposal and considered that separate accounting data should be provided by individual DNs where a single entity conducts more than one business.
- 5.317. One shipper/supplier considered that efficiency incentives would be weakened for owners of multiple DNs if they were not required to produce separate regulatory accounts. In a similar respect, a potential purchaser was of the opinion that further attention should be given to regulatory accounting guidelines to ensure that transparency is retained in dealings between the NTS and RDNs.
- 5.318. In contrast, Transco considered that the regulatory accounting provisions should be amended to require auditors to provide a 'fairly presents' opinion as opposed to a 'true and fair' opinion regarding the accounts of the NTS and each RDN. In this respect, NGT was of the view that the 'fairly presents' requirement should relate to the licensed business as a whole.

5.319. In addition, NGT considered that the requirement to produce current cost regulatory accounts and an unaudited interim regulatory profit and loss account should be removed from this licence condition. NGT also highlighted that the business definitions, in relation to the DNs and the NTS, and the implementation dates would need to be reviewed.

Ofgem's proposals

5.320. Consistent with the majority of respondents, Ofgem continues to consider its proposals to be appropriate.

5.321. Ofgem proposes that the provisions currently set out in the amended standard condition should be amended to ensure the submission of regulatory accounts for each separate RDN business and then placed in a standard special condition for all NTS and DN-GTs. The proposed drafting for this Condition (Standard Special Condition A30) is provided for comment in Appendix 7B.

5.322. The drafting contained within Standard Special Condition A30 reflects Transco's licence as it currently stands. In this respect it is important to note that changes may be required to this draft condition to reflect developments occurring through the DPCR 4 process.

5.323. Ofgem notes that the requirement to produce current costs regulatory accounts and an unaudited interim regulatory profit and loss account is being revised through the DPCR 4 process. It is Ofgem's intention that regulatory reporting licence conditions should be consistent across all regulated businesses and that following the DPCR 4 the regulatory accounts reporting requirements may be amended to

- ◆ remove the requirement to produce current costs regulatory accounts and an unaudited interim regulatory profit and loss account;
- ◆ update the regulatory accounts format in line with the most recent changes to companies legislation; and
- ◆ require the auditors to move to a "fairly presents" opinion instead of a "true and fair view" opinion.

5.324. As discussed in Chapter 4, to address the issue of LNG:

- ◆ this standard special condition has reverted to the references to LNG storage facilities contained in the standard conditions designated by the Secretary of State under the Utilities Act; and
- ◆ a new NTS Special Condition has been introduced to “augment” this standard special condition with LNG related provisions (Special Condition C1, paragraph 9). This is discussed in further detail in Chapter 6.

5.325. The amended standard condition would then revert to the Designated Standard Condition for all NTS and DN-GTs which would then be switched off.

5.326. This condition needs to be considered to ensure intra-company dealing is appropriately treated between Transco’s NTS and RDNs. As Transco’s NTS and DN businesses will be internal business units of a single company it will not be subject to the provisions of paragraph 1 in relation to intra-company dealings.³⁶ It may therefore be necessary to make further changes to this condition to ensure that Transco’s RDNs are required to maintain accounting and reporting records that permit the Transco NTS licensee to fulfil its obligations (and vice versa). Such a change could be given effect through changes to special conditions. Ofgem intends to discuss this matter further at an upcoming DISG meeting.

5.327. Ofgem invites respondents’ views on its proposals for Amended Standard Condition 30. Following consideration of respondents’ views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

³⁶ Similarly, Transco NTS and RDNs would not be subject to the provisions of paragraph 9 of Special Condition C1 (the amended NTS version of paragraph 1 of Standard Condition A30) for intra-company dealings.

Standard Condition 30A – Change of Financial Year

Description

- 5.328. Where the licensee changes its financial year in relation to its statutory accounts, it must provide notice to the Authority specifying the new dates for the current and subsequent financial years which will continue in force unless revoked by the licensee by further notice.

September document

- 5.329. In the September document Ofgem detailed that it was minded not to propose any modifications to this condition so that Standard Condition 30A would continue to apply to all GT licences including NTS and DN GTs.

Respondents' views

- 5.330. Ofgem did not receive any comments in relation to this proposal.

Ofgem's proposals

- 5.331. Ofgem continues to consider it appropriate not to propose any modifications to this condition so that Standard Condition 30A would continue to apply to all GT licences including NTS and DN GTs. The wording of this Condition is provided in Appendix 7A.
- 5.332. However, it should be noted that changes may be required to this condition to reflect developments occurring through the DPCR 4 process, in particular relating to the regulatory accounts provisions.
- 5.333. Ofgem invites respondents' views on its proposals for Standard Condition 30A. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be consulted upon in February 2005. Further consultation may take place during this period through the DISG meetings.

Amended Standard Condition 31 – Supply Point Administration Services

Description

- 5.334. Amended Standard Condition 31 obliges the licensee to establish, operate and maintain an information service with a register that provides information regarding the identity of the relevant gas shipper, the type of equipment installed and an accurate address of all domestic premises. This Condition also contains an obligation to provide information on gas pressure for parties who may require connecting pipelines and other information as needed.

September document

- 5.335. As part of the informal licence consultation, Ofgem considered that the amended form of Standard Condition 31 should apply to the NTS and DN-GT licensees and was minded to introduce a standard special condition in NTS and DN-GT licences dealing with the matters in this condition.

Respondents' views

- 5.336. One shipper/supplier agreed with Ofgem's proposals and considered that obligations in relation to the register and maintenance of domestic supply point data would be vital in a divested industry structure. NGT considered that this condition should be amended to only apply where a GT has more than one domestic customer.

Ofgem's proposals

- 5.337. Following consideration of respondents' views on this condition Ofgem continues to consider that the provisions of Standard Condition 31 should apply to all GTs following DN sales. Ofgem believes that these provisions should apply regardless of whether there are domestic customers connected to the licensee's network as they relate to both domestic and non-domestic customers.
- 5.338. Ofgem therefore proposes that the provisions contained in Amended Standard Condition 31 (which incorporates additional provisions to the Designated Standard Condition) should be set out in a standard special condition applicable to all NTS and DN-GTs. The proposed drafting for this Condition (Standard Special Condition A31) is provided for comment in Appendix 7B.

- 5.339. Amended Standard Condition 31 will then revert to the Designated Standard Condition in the licences of all NTS and DN-GTs, which will then be switched off.
- 5.340. Ofgem invites respondents' views on its proposals for Amended Standard Condition 31. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Part C

Amended Standard Condition 32 – Interpretation of Section C

Description

- 5.341. This condition sets out the definition of 'permitted purpose' activities which, through the operation of other conditions, the licensee is authorised to pursue in the conduct of its business.
- 5.342. Permitted purpose is used to define the scope of the obligations set out in Section C of the licence and certain Special Conditions. Amended Standard Condition 32 in Transco's licence defines "permitted purpose" as including Transportation and LNG Storage Business, Meter Business and Meter Reading Business.

September document

- 5.343. In the informal licence consultation Ofgem considered that to reflect the nature of the business, the amended form of Standard Condition 32 should be retained as standard special conditions in respect of Transco's NTS and RDNs but not for the other DNs. In the case of the other DNs, Ofgem considered that amendments should be made separate to the DN Sales process.

Respondents' views

- 5.344. One potential purchaser considered that decisions regarding “permitted purpose” provisions would be dependent upon the outcome of decisions regarding metering and LNG storage.
- 5.345. Another response received, on behalf of a shipper/supplier, set out that it was unclear why Ofgem would accept the outlined approach as the DNs are likely to be required to provide most of the services that were previously the responsibility of Transco.

Ofgem’s proposals

- 5.346. As discussed in Chapter 4, Ofgem has decided that provisions related to metering and meter reading should sit within the licences of all NTS and DN-GTs. As such, it is necessary for the amended version of this Condition (insofar as it relates to these activities) to apply to all DN and NTS-GT licensees.
- 5.347. Ofgem therefore proposes that the provisions contained in Amended Standard Condition 32, other than those relating to LNG Storage, should be placed in a standard special condition applicable to all DN and NTS-GT licences. It has also been necessary to amend cross references within this Condition. The proposed drafting for this Condition (Standard Special Condition A32, Definition of Permitted Purpose) is provided for comment in Appendix 7B.
- 5.348. As discussed in Chapter 4, to address the issue of LNG, a new NTS Special Condition has been introduced to “augment” this standard special condition with LNG related provisions (Special Condition C1, paragraph 10). This is discussed in further detail in Chapter 6.
- 5.349. Amended Standard Condition 32 will then revert to the Designated Standard Condition in the licences of NTS and DN-GTs, which will then be switched off.
- 5.350. Further consideration will need to be given to whether there is a need to modify the definition of Permitted Purposes within the NTS and RDN licences for the purposes of business separation. Ofgem will take its proposals, in this area, to DISG. (check when Transco drafting arrives)
- 5.351. Ofgem invites respondents’ views on its proposals for Amended Standard Condition 32. Following consideration of respondents’ views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG

meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 33 – Designated Registrar of Pipes

Description

- 5.352. The Authority may, by notice, designate the licensee as the “Designated Registrar of Pipes”, obliging it to establish, maintain and operate or procure the establishment, operation and maintenance of a service to be known as the Main Administration Service within the area described in the designation notice.
- 5.353. There is currently no Designated Registrar of Pipes. The condition is included in Transco’s existing GT licence, but requires a direction from the Authority, following consultation, in order for Transco to be obliged to comply with it.

September document

- 5.354. In the informal licence consultation Ofgem set out that it was minded not to propose any modifications to this condition and, in effect, Standard Condition 33 would continue to apply to all GT licences. The Authority would therefore retain the ability to designate any GT as the Designated Registrar of Pipes.

Respondents’ views

- 5.355. Eight responses were received in relation to the proposals regarding the Designated Registrar of Pipes.
- 5.356. Gas Industry Safety Group considered that the divested industry structure that would be in place following a potential DN sale has strengthened the case for switching on this condition. One IGT and two further respondents were also of the opinion that the activation of this condition would have key benefits in that it would increase accuracy and consistency of records and improve the ease of access to such records. Although, these three respondents qualified their support by stating that benefits associated with the Authority issuing such a direction would need to be weighed against the additional costs of funding it.

- 5.357. In a similar respect, Gas Industry Safety Group asked for clarification regarding the way in which an amendment in this respect would be funded, while a further respondent considered that the registrar should be independent and funded jointly by all DNs, the NTS and IGTs.
- 5.358. In contrast to these responses, two potential purchasers considered that the status quo should be maintained with respect to the Designated Registrar of Pipes. Of these, one was of the opinion that future arrangements would be sufficient to ensure that the NTS and DNs update, maintain and, where appropriate, share accurate records of their pipeline systems.
- 5.359. NGT was also of the opinion that a registrar of pipes should not be designated and suggested that it would be difficult to ensure that accurate and consistent methods of data collection were employed under the provisions of this condition. As such, NGT stated that the records may be of limited reliability and that given the costs associated with designating a registrar of pipes it would not be appropriate to switch on this condition.
- 5.360. One IGT and one shipper/supplier considered that such a change would be outside of the scope of the DN sales process and that it would be more appropriate to discuss a modification of this nature as part of a separate consultation.

Ofgem's proposals

- 5.361. Ofgem continues to consider it appropriate for Standard Condition 33 to apply to all NTS and DN-GTs which will provide the Authority with the flexibility to appoint a Registrar of Pipes (or several such Registrars) should this be considered appropriate. Standard Condition 33 will therefore remain unchanged, and continue to apply to all GT licensees including all NTS and DN-GTs. The wording of this Condition is provided in Appendix 7A.
- 5.362. Ofgem has not yet reached a decision as to whether the Authority will be exercising its powers to appoint such a Registrar(s) as part of the DN Sales process, but will carry out a full consultation before deciding to make any such direction. The issue of cost allocation would be considered as part of any such consultation. Ofgem intends to discuss these conditions at a future DISG meeting.

5.363. Ofgem invites respondents' views on its proposals for Standard Condition 33. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 38 – Availability of Data Formats

Description

5.364. Where a licensee uses standard file formats for transferring data for any purpose set out in the licensee's Network Code it is required to make those standard file formats and associated definitions of data available free of charge to shippers and GTs for use in connection with their licensed activities.

September document

5.365. Ofgem considered that it would be necessary to amend Standard Condition 38 to take account of the new arrangements proposed under the UNC. As such, Ofgem stated that a modified version of Standard Condition 38 should be introduced as a standard special condition in the licences of all NTS and DN GTs in order to accommodate this new commercial regime.

Respondents' views

5.366. One shipper/supplier agreed that it would be necessary to include this provision in the licences of the NTS and DN-GTs to ensure they are able to share file formats.

Ofgem's proposals

5.367. Following development of the proposals regarding the UNC since the September document was published Ofgem now considers it to be appropriate for the standard form of this condition to apply to all DN and NTS GT licence holders. Ofgem considers that the wording contained in the condition offers sufficient

flexibility to ensure that the relevant file formats can be shared with relevant persons subject to the drafting of the Network Code³⁷.

5.368. The wording of this Condition is provided in Appendix 7A.

5.369. Ofgem invites respondents' views on its proposals for Standard Condition 38. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Amended Standard Condition 39 – Restriction on Use of Certain Information and the Independence of the Transportation Business

Description

5.370. Amended Standard Condition 39 prevents the flow of information between the transportation business, the trading business, and pursuant to the changes brought about through the Review of Gas Metering Arrangements (RGMA), the licensee's Meter-Related Services Business and Meter Reading Business.

5.371. The condition obliges the licensee to use its best endeavours to secure that no information related to, or derived from, its transportation business is disclosed for the purposes or benefit of its trading business, its meter related services business, its meter reading business or any affiliate or related undertaking of the licensee.

5.372. In this licence condition the transportation business includes LNG storage arrangements but the Authority has the ability to omit these provisions through the procedures contained within this Condition.

³⁷ Ofgem is currently consulting on proposed modifications to this condition. Any such changes to the Designated Standard Condition that take effect prior to the Section 8AA consent process will need to be taken into consideration.

September document

- 5.373. In its informal licence consultation Ofgem considered that it would be necessary to retain the obligations contained in this condition within the NTS and DN GT licences as a standard special condition.
- 5.374. Ofgem also detailed that in Ofgem's conclusions document regarding offtake arrangements, the Authority was minded to require legal and structural separation between Transco's NTS and RDNs. As such, consideration would need to be given to the additional requirements that may need to be put in place to support this aspect of information separation.
- 5.375. Ofgem proposed that this could be achieved either through modifications to Amended Standard Condition 39 or the creation of Special Conditions applicable to the NTS and RDN-GT licensees.
- 5.376. Ofgem considered that this condition, as well as others, may require further modifications to deal with potential competition concerns which may arise when issues associated with separation requirements in relation to potential purchasers have been fully considered.

Respondents' views

- 5.377. Six respondents submitted comments in relation to proposals regarding Amended Standard Condition 39. These included three potential purchasers, two shipper/suppliers and a further respondent. Of these, all were supportive of the proposals to amend this condition to ensure that no party would be able to discriminate in favour of a related business.
- 5.378. Two potential purchasers considered that the most important issue to address concerned the possibility for the NTS to exercise undue discrimination in favour of its RDNs. Of these, one considered that issues in this regard could be addressed through the inclusion of non-discrimination conditions within the NTS and DN-GT licences, combined with structural separation of the NTS and RDN-GTs and the implementation of appropriate compliance regimes. One shipper/supplier and two further respondents also considered that it was crucial that all possibilities, in which discrimination in favour of affiliates may occur, were addressed.

- 5.379. In addition, one respondent was of the opinion that while there should be a general prohibition on the exercise of undue discrimination by the NTS or DN-GTs in relation to affiliates the condition should also include an extended “without limitation” list of prohibited actions.
- 5.380. A potential purchaser suggested that if any additional licence modifications were required to accommodate issues that arise with respect to competition, these should be developed through industry consultation.
- 5.381. As a general point, a further potential purchaser considered that the ring-fencing conditions that currently have effect within the licence should either be amalgamated or incorporated into successive conditions for ease of reference.

Ofgem’s proposals

- 5.382. As set out in Chapter 4, Ofgem considers that it is appropriate to update the business separation requirements to align the gas business separation requirements with those that apply in electricity. Ofgem also considers that it is necessary to introduce new Special Conditions to apply to Transco’s NTS and RDN businesses to ensure no undue discrimination. These are set out in Chapter 6.
- 5.383. Ofgem believes that this condition should be switched off and replaced with new provisions:
- ◆ a new Standard Special Condition (A33) that reflects the arrangements for electricity DNOs in terms of preventing preferential dealings between NTS and DN GTs and their affiliated shipping or supply businesses; and
 - ◆ new Special Conditions for Transco that put in place the same regime between NTS and DNs, and also certain additional Special Conditions to emulate the effect of legal separation between NTS and DNs. The drafting of this condition will be provided to DISG.
- 5.384. Ofgem therefore proposes that Amended Standard Condition 39 will revert to its designated form and then be switched off. The proposed new licence conditions are described in more detail in Chapter 6.

- 5.385. Ofgem notes that Amended Standard Condition 39 contains certain additional provisions relating to storage and metering which have no equivalent within the electricity DNO regime. In making the proposed changes, it will be important to accommodate these arrangements.
- 5.386. Ofgem invites respondents' views on its proposals for Amended Standard Condition 39. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation will take place during this period through the DISG meetings.

Standard Condition 40 – Appointment of Compliance Officer

Description

- 5.387. The licensee is obliged to ensure that at all times it employs a competent person (the Compliance Officer) for the purpose of facilitating compliance with Standard Condition 39. The licensee is also obliged to furnish to the Authority and publish in the form and manner directed by the Authority a report on the Compliance Officer's activities.

September document

- 5.388. As part of the informal licence consultation, Ofgem considered that it would be necessary to retain this obligation in the NTS and DN-GT licences and that it would be necessary to consider any consequential amendments to this standard condition following the modifications to Amended Standard Condition 39.

Respondents' views

- 5.389. Ofgem did not receive any comments in relation to this proposal.

Ofgem's proposals

- 5.390. As with Amended Standard Condition 39, Ofgem now proposes to switch off the provision in order to update the business separation regime to reflect that arrangements that apply in electricity.
- 5.391. The proposed new licence conditions are described in more detail in Chapter 6 and is reflected in the drafting provided for Standard Special Condition A34, in Appendix 7B.
- 5.392. Ofgem invites respondents' views on its proposals for Standard Condition 40. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be consulted upon in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 41– Prohibition of Cross-Subsidies

Description

- 5.393. This condition requires the licensee to procure that its transportation business does not give or receive any cross subsidy to or from any other business of the licensee or of an affiliate or related undertaking of the licensee.

September document

- 5.394. Ofgem detailed, as part of the informal licence consultation that it was minded not to propose any modifications to this condition so that Standard Condition 41 would continue to apply to all GT licences including NTS and DN-GTs.

Respondents' views

- 5.395. Two shipper/suppliers and a further respondent considered that the prohibition of cross-subsidies between DNs contained within the same trading group would be fundamental in a post-DN sales environment.

- 5.396. One potential purchaser was of the opinion that the issue of cross-subsidies could be addressed through the inclusion of a clause within the regulatory accounts to require an increased level of reporting regarding material transactions between RDN-GTs and other parts of the NGT group.
- 5.397. NGT was supportive of the continued operation of this provision provided that it would not prevent the continuation of its current purchasing arrangements.

Ofgem's proposals

- 5.398. Ofgem has made clear that each DN is to have a separate price control and separate regulatory accounts will be required from each DN business. Ofgem is satisfied that these requirements along with the prohibition of cross-subsidies contained in this provision should be sufficient to protect the interests of customers.
- 5.399. Following consideration of respondents' views, Ofgem proposes that Standard Condition 41 be switched off and replaced with a standard special condition that includes an additional provision. The additional provision would clarify that, in the event that the licensee's transportation business contains more than one transmission and/or distribution business, the prohibition on cross subsidies applies in respect of each individual transmission and/or distribution business.
- 5.400. The proposal to amend Standard Condition 41 is not reflected in the attached licence drafting. Ofgem is currently developing detailed proposals. Ofgem intends to present an initial draft of these proposed licence conditions to the DISG and to invite comments on the drafting.
- 5.401. Ofgem invites respondents' views on its proposals for Standard Condition 41. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Amended Standard Condition 45 – Undertaking from an Ultimate Controller

Description

5.402. Amended Standard Condition 45 sets out the requirement on the licensee to obtain a legally enforceable undertaking from each and every person who is an ultimate controller of the licensee in the form specified by the Authority, that the ultimate controller will:

- ◆ refrain from any action; and
- ◆ procure that any person whom it controls will refrain from any action,

which would then be likely to cause the licensee to be in breach of any of its obligations under the Gas Act or licence.

5.403. Transco's existing licence condition is an amended standard condition. Previous amendments to this condition have incorporated an alternative definition of ultimate controller to that set out in the standard condition. The definition has subsequently reverted to the standard definition and, as such, this condition is now in the standard form.

September document

5.404. In its informal licence consultation Ofgem detailed that it was minded to adopt the standard form of Standard Condition 45 in all NTS and DN-GT licences i.e. Standard Condition 45 would operate within all GT licences.

Respondents' views

5.405. NGT supported the inclusion of the standard form of Standard Condition 45 in all NTS and DN-GT licences.

Ofgem's proposals

5.406. Ofgem proposes to adopt the standard form of Standard Condition 45 in all NTS and DN-GT licences. The wording of this Condition is provided in Appendix 7A.

5.407. Ofgem invites respondents' views on its proposals for Amended Standard Condition 45. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Amended Standard Condition 47– Indebtedness

Description

5.408. This condition prevents the licensee from incurring inappropriate indebtedness or giving any form of security or guarantee unless it is on an arm's length basis, on normal commercial terms and for permitted purposes and, where relevant, in accordance with Standard Condition 29 (disposal of assets). Otherwise, new (i.e. all but "pre-relevant date"³⁸) indebtedness, without the prior written consent of the Authority is prohibited.

5.409. The condition requires the prior written consent of the Authority for transfers, leases etc, of any asset, right, sum or benefit etc. to any affiliate or related undertaking subject to certain exceptions.

September document

5.410. In the informal licence consultation Ofgem detailed that it was minded to revert to the standard form of Standard Condition 47 in all NTS and DN-GT licences with the associated standard Cross-Default Obligation provisions. Ofgem also set out that the grant of consents to Transco in relation to pre-relevant date indebtedness and Cross-Default Obligations would be preserved to the extent that such obligations remain outstanding. As a result, Special Condition 5 would no longer be needed.

³⁸ The relevant date is defined in Transco's licence as 13 December 1999, which is the date under which the Scheme of Arrangements became effective under section 425 of the Companies Act 1985.

Respondents' views

- 5.411. NGT expressed its support for this proposal provided that Ofgem will grant consent to permit NGT to continue pre relevant date indebtedness levels.

Ofgem's proposals

- 5.412. Ofgem continues to consider it appropriate to revert to the standard form of Standard Condition 47 in all NTS and DN-GT licences with the associated standard Cross-Default Obligation provisions. However, there is a need to modify the condition to allow for changes to conform NTS and DN-GT licences to the standard form of this condition proposed for electricity distribution licences. In particular, changes will be made to include the use of Fitch credit-ratings (discussed later in this Chapter under Special Condition 4) and cash lock up.
- 5.413. The cash lock up provisions require that, with certain limited exceptions, the licensee shall not, without the prior written consent of the Authority, transfer, lease, licence or lend any sums, assets, rights or benefit as allowed under paragraph 1, if the licensee ceases to hold an investment grade credit rating or if the licensee's lower or lowest rating is at the minimum investment grade level (BBB-/Baa3) and is placed under review for possible downgrade or on credit watch with negative implications or its rating outlook is changed to negative from positive or stable. Where this is the case and until such time as all the licensee's ratings are restored to a level above the trigger, the licensee shall not transfer, lease, licence or lend any sums, assets, right or benefit, without prior written consent of the Authority following disclosure of all material facts, other than by the methods specified.
- 5.414. These provisions are currently being consulted upon as changes to the Distribution Price Control Review (DPCR4), and are proposed for inclusion within GT licences to ensure consistency across network businesses. Some further changes may be made to the text appearing in Appendix 7B.
- 5.415. Therefore the provisions contained in the Designated Standard Condition with the necessary amendments (as discussed above) will be placed in a standard special condition applicable to all NTS and DN-GTs. The proposed drafting for

this Condition (Standard Special Condition A39) is provided for comment in Appendix 7B.

- 5.416. The consents currently in place relating to pre relevant date cross defaults will be preserved and therefore Special Condition 5 will no longer be needed.
- 5.417. Ofgem invites respondents' views on its proposals for Amended Standard Condition 47. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Standard Condition 48 – Last Resort: Payment Claims

Description

- 5.418. Standard Condition 48 sets out the circumstances under which the licensee is required to increase its transportation charges in order to compensate any gas supplier which claims for losses that it has incurred in complying with a last resort supply direction. Where the licensee receives from a claimant supplier a valid claim for a last resort supply payment, it is required to make a consequential increase in its transportation charges to such an extent as it reasonably estimates to be appropriate to secure that such consequential increase in its revenue equals the specified amount of the claim by the supplier.

September document

- 5.419. In its informal licence consultation Ofgem was minded not to propose any modifications to this condition so that Standard Condition 48 would continue to apply to all GT licences including NTS and DN-GTs.

Respondents' views

- 5.420. One shipper/supplier acknowledged that this condition would need to be retained but was of the opinion that Ofgem would need to ensure that this

condition did not adversely impact upon the requirements contained under Amended Standard Condition 4.

- 5.421. This condition has also been considered by DISG members. At the DISG, a representative for a potential purchaser considered that the reasonable endeavours obligation regarding the frequency of changes to the charging methodology should be amended to reflect the provisions contained within this condition.

Ofgem's proposals

- 5.422. Ofgem continues to consider it to be appropriate for this condition to apply to all GT licences including NTS and DN-GT licence holders. Ofgem recognises that if the provisions of this clause need to be enacted it may be necessary for a GT to change its transportation charges on a date other than those specified in Standard Special Condition A4. We consider that such situations may fall outside of the reasonable endeavours obligation and that such additional changes may be unavoidable in order to ensure that suppliers are protected in respect of a last resort order.
- 5.423. Ofgem therefore proposes to adopt the standard form of Standard Condition 48 in all GT licences including NTS and DN-GTs. The wording of this Condition is provided in Appendix 7A.
- 5.424. Ofgem invites respondents' views on its proposals for Standard Condition 48. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Conditions

Special Condition 1 – Interpretation and Construction

Description

- 5.425. Special Condition 1 sets out some of the rules for the interpretation and construction of the Special Conditions. Unless the context requires otherwise, words and expressions used in the standard conditions of the licence have the same meaning as in the Special Conditions. It should be noted that some of the Special Conditions also set out particular definitions or interpretations which are specific to the condition in question.

September document

- 5.426. As explained above, in the September document Ofgem detailed that it was likely that there would need to be a new standard special condition for NTS and DN-GT licensees dealing with issues of definition, interpretation and construction. In addition, Ofgem considered that it may be necessary to include further definitions within Special Conditions applicable to individual licensees.

Respondents' views

- 5.427. Ofgem did not receive any comments in relation to this proposal.

Ofgem's proposals

- 5.428. As a result of the proposed changes to a number of the Special Conditions currently within Transco plc's Special Conditions, the definitions within Special Condition 1 are no longer required, and as such these provisions have been deleted.
- 5.429. As stated earlier in this chapter, the provisions of Amended Standard Condition 1, which currently provides definitions across NTS and DN-GTs, will become part of a new standard special condition (Standard Special Condition A3), which will be supplemented by additional definitions as required. However, Ofgem remains of the view that it may be necessary to include further definitions within Special Conditions applicable to individual licensees.

5.430. However, as stated in the September document, the definitions to be included in these new licence conditions will need to follow the restructuring of the licence and the commercial regime as a whole. As such, new definitions may need to be discussed through the DISG.

5.431. Ofgem invites respondents' views on its proposals for Special Condition 1. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 2 – Restriction on Activity and Financial Ring-Fencing

Description

5.432. This condition prohibits the licensee from undertaking any business other than:

- ◆ the Transco Business³⁹;
- ◆ a business for which the Authority has given express consent; or
- ◆ a “de minimis” business.

5.433. The condition states that the licensee shall not, without the written consent of the Authority, hold or acquire shares or other investments of any kind except in prescribed circumstances.

5.434. The condition also imposes a reasonable endeavours obligation on the licensee to cease to conduct and carry on a business or activity which it was conducting or carrying on at the relevant date and which it would otherwise be prohibited by this condition from conducting. The licensee is required to submit a report to the Authority setting out its endeavours to comply with this condition.

³⁹ Including Transportation and LNG Storage, the Metering Business and the Meter Reading Business. The Condition provides that LNG storage may be excluded from the scope of the condition if the Authority so directs.

September document

- 5.435. As part of its informal licence consultation, Ofgem proposed that this Special Condition should be removed from Transco's existing GT licence and Standard Condition 43 (Restrictions on Activity and Financial Ring-Fencing) used in its place.
- 5.436. Ofgem also set out that Transco's "permitted purpose" would be defined as in Amended Standard Condition 32. Ofgem recognised that it may be necessary to supplement Designated Standard Condition 43 with one or more Special Conditions in order to retain the definition of "investment" such that for the purposes of calculating an "investment", account is taken of income received by the licensee in respect of such investment. Special Condition 2 would then be modified out of the licence.

Respondents' views

- 5.437. NGT responded to the proposals included in reference to Special Condition 2 and supported the removal of this condition and corresponding reinstatement of Standard Condition 43 within the NTS-GT licence.
- 5.438. NGT considered that permitted purpose activities would need to be amended within the NTS-GT licence in order to reference the LNG storage business.
- 5.439. NGT also supported the retention of the definition of investment included within the condition as this would be necessary in order to enable de minimis business investment to be calculated.

Ofgem's proposals

- 5.440. Ofgem remains of the view that the provisions of Standard Condition 43 should replace the wording of this condition. However, rather than applying Standard Condition 43 as currently drafted, a standard special condition would be introduced containing the provisions contained in this condition, with necessary amendments which:
- ◆ retain the definition of "investment" previously applied in Special Condition 2 such that account would continue to be taken of income received by the licensee in respect of such investment; and

- ◆ replace “transportation business” with a reference to the definition of “permitted purpose” in what is currently Amended Standard Condition 32.

5.441. These provisions are set out in a standard special condition applicable to all NTS and DN-GTs. The proposed drafting for this Condition (Standard Special Condition A36) is provided for comment in Appendix 7B.

5.442. As stated in Chapter 4, Ofgem continues to be of the view that SOMSAs should not be regulated. However, it will be necessary to amend standard special condition A36 – Restriction on Activity and Financial Ringfencing to accommodate income from new service agreements such as SOMSAs. As such, a new RDN Special Condition has been drafted (Special Condition E1) to adjust the de minimis percentage restriction for a specified period such that in aggregate, de minimis turnover and investments do not exceed a specified amount for that period. These new conditions are discussed further in Chapter 6.

5.443. Ofgem invites respondents’ views on its proposals for Special Condition 2. Following consideration of respondents’ views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 3 – Availability of Resources

Description

5.444. This condition states that the licensee shall ensure that it has sufficient resources to carry out its Transportation and LNG Storage business properly and efficiently and to comply with all of its relevant obligations. The licensee is also obliged to submit to the Authority, each year, a Board approved certificate relating to the adequacy of its resources to carry on the activities authorised by the licence.

5.445. This condition also includes a requirement for a specific certificate before any dividend or distribution may be paid or made and prohibits such dividends or distributions if the requisite certificate is not provided. As part of DPCR4 it is proposed to amend this provision to extend its requirements to the repurchase of shares. To the extent this is not reflected in Appendix 7B, it will be introduced at the Section 23 stage.

September document

5.446. In the informal licence consultation Ofgem considered that the provisions contained within this licence condition should continue to apply to all NTS and DN-GTs through the creation of a standard special condition.

Respondents' views

5.447. NGT expressed support for the retention of this condition within each GT licence and considered that the obligation should be amended to reflect the view that the LNG storage business should only apply to the NTS.

Ofgem's proposals

5.448. Having considered NGT's response, Ofgem continue to consider that Special Condition 3 should continue to apply as a standard special condition.

5.449. In the light of the decision that LNG storage businesses should only apply to the NTS, Ofgem considers that this licence condition should become a standard special condition applicable to all NTS and DN-GTs (excluding LNG storage references). The proposed drafting for this Condition (Standard Special Condition A37) is provided for comment in Appendix 7B.

5.450. As discussed in Chapter 4, to address the issue of LNG:

- ◆ this standard special condition has reverted to the references to LNG storage facilities contained in the standard conditions designated by the Secretary of State under the Utilities Act; and
- ◆ a new NTS Special Condition has been introduced to "augment" this standard special condition with LNG related provisions (Special

Condition C1, paragraph 12). This is discussed in further detail in Chapter 6.

- 5.451. Ofgem invites respondents' views on its proposals for Special Condition 3. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 4 – Investment Grade Credit Rating as Issuer of Corporate Debt

Description

- 5.452. This condition obliges the licensee to use all reasonable endeavours to maintain an investment grade credit rating and is based upon Standard Condition 46.

September document

- 5.453. In its informal licence consultation Ofgem was minded to remove this condition and reinstate Standard Condition 46, as designated by the Secretary of State, for all GT licences.
- 5.454. Ofgem also considered, as an alternative, whether a standard special condition should be introduced to include other rating agencies as well as Standard & Poor's and Moody's.

Respondents' views

- 5.455. Four respondents submitted comments on this proposal. Of these, a potential purchaser and NGT supported the proposal to revert to Standard Condition 46. NGT also noted that in the event that a licensee does not have any external debt it should remain the case that the obligation to obtain a credit rating should not apply in these circumstances.

5.456. One potential purchaser supported Ofgem's proposal to introduce a Standard Special condition including other rating agencies as well as Standard & Poor's and Moody's. A second potential purchaser also supported the proposal to include additional ratings agencies in principle but was of the opinion that such an amendment would be outside of the scope of the DN sales project. A shipper/supplier was also unsure whether this amendment should be included as an appropriate modification in relation to DN sales.

Ofgem's proposals

5.457. Ofgem agrees that the inclusion of Fitch or other rating agencies as well as Standard & Poor's and Moody's is not directly related to the DN sales process. Furthermore, Ofgem notes that significant modifications to the licence that are not related to the DN sales process would not be appropriate within this framework. However, Ofgem considers that, as part of the DN sales licence review process, it is justified in performing relatively minor modifications to "tidy up" the drafting or introduce minor adjustments to ensure promotion of consistent Ofgem policy across the electricity and gas sectors where appropriate.

5.458. Given that those respondents that commented specifically on the proposed change, were in favour of such a change, and given the relatively minor nature of this change, Ofgem is minded to implement this change as part of the Section 8AA process (and associated Section 23 notice). Ofgem is therefore proposing to introduce a standard special condition, based on designated Standard Condition 47, and to modify this to include Fitch rating agency as well as Standard & Poor's and Moody's. The proposed drafting for this Condition (Standard Special Condition A38) is provided for comment in Appendix 7B. Respondents are invited to set out any policy concerns regarding this proposed change in a response to this document.

5.459. Ofgem invites respondents' views on its proposals for Special Condition 4. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be

published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 5 – Cross-Default Obligations

Description

- 5.460. This condition prohibits the licensee from entering into or continuing with any cross-default obligations without the prior consent of the Authority.

September document

- 5.461. As part of the informal licence consultation, Ofgem detailed that it was minded to revert to Standard Condition 47, which incorporates a prohibition on cross-default obligations, for both NTS and DN-GTs. As such, Special Condition 5 would no longer be needed.

Respondents' views

- 5.462. NGT expressed support for Ofgem's proposal to remove Special Condition 5 and reinstate Standard Condition 47 in its place. NGT clarified, however, that its support was conditional on the retention of existing arrangements in relation to cross-default provisions.

Ofgem's proposals

- 5.463. Ofgem remains of the view that this Special Condition should be removed from Transco's existing GT licence. As discussed earlier in this chapter, a standard special condition has been introduced (Standard Special Condition A39), which reflects the wording of Designated Standard Condition 47. As such, Special Condition 5 (and its associated provisions) has been removed from the draft licence.
- 5.464. As stated in the September document, the grant of consents to Transco in relation to pre relevant date indebtedness would be preserved to the extent that such obligations remain outstanding.
- 5.465. Ofgem invites respondents' views on its proposals for Special Condition 5. Following consideration of respondents' views, where necessary and

appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 9D – Restriction of Prices for LNG Storage Services

Description

- 5.466. This condition sets out the charges which the licensee may apply for the supply of LNG storage services at certain sites on the NTS network. The licensee may not deviate from those charges except with the Authority's prior written consent.

September document

- 5.467. As part of the informal licence consultation Ofgem referred respondents to its comments relating to the treatment of LNG generally set out in relation to Amended Standard Condition 4 above. Ofgem considered that it could not propose changes to this condition until the outcome of this consultation was clear and a decision regarding the treatment of LNG had been reached.

Respondents' views

- 5.468. Ofgem did not receive any comments in relation to this proposal.

Ofgem's views

- 5.469. As discussed earlier in this document, Ofgem is minded to include current licence obligations relating to LNG storage, within Transco's NTS-GT licence only. As such, Ofgem is of the view that this Special Condition should be a Special Condition applicable to Transco's NTS only. The proposed drafting for this Condition (Special Condition C3) is provided for comment in Appendix 7B.
- 5.470. Ofgem invites respondents' views on its proposals for Special Condition 9D. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales

then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 17 – Operational Guidelines for Balancing

Description

- 5.471. This condition requires the establishment of operational guidelines consistent with the Network Code, specifying the particular balancing measures that the licensee expects to take. This condition also provides for the publication and modification of the guidelines and the preparation of reports to the Authority.

September document

- 5.472. In the informal licence consultation Ofgem proposed that this condition could be deleted and superseded by the provisions of existing Special Condition 27 which would provide for the establishment of a System Management Principles Statement.

Respondents' views

- 5.473. NGT expressed support for the proposal to remove Special Condition 17 from the licence and replace it with Special Condition 27.
- 5.474. This condition has been presented at DISG. One shipper/supplier considered that it was of crucial importance that Special Condition 27 would correctly allocate responsibilities between the NTS and DN-GTs and, in particular, that the NTS should only retain responsibility for residual energy balancing.

Ofgem's views

- 5.475. Ofgem remains of the view that this condition should be deleted and superseded by the provisions of existing Special Condition 27. The proposals regarding Special Condition 27 are discussed in more detail below, and reflected in the drafting of Special Condition C5, which is provided for comment in Appendix 7B.

- 5.476. Ofgem invites respondents' views on its proposals for Special Condition 17. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 18 – Conveyance to Independent Systems

Description

- 5.477. Special Condition 18 requires that the average charge for the conveyance of gas to independent systems should be no more than the average charge for conveyance to all premises in Great Britain supplied with that type of gas.

September document

- 5.478. In the informal licence consultation Ofgem detailed that it had published an open letter on 6 August informing interested parties that it would consider the necessary amendments to this condition, as a result of the network sales, and issue its subsequent conclusions. As such it proposed to progress the issues associated with Special Condition 18 separately to the informal consultation.

Respondents' views

- 5.479. One potential purchaser and a shipper/supplier submitted a response in relation to this proposal. Both expressed interest in relation to the resolution of issues regarding this condition.

Ofgem's views

- 5.480. In the process of considering the licence changes that may be required to facilitate the commercial and regulatory arrangements that would be in place following DN Sales, the Authority has asked the Department of Trade and Industry (DTI) to review Special Condition 18 in Transco plc's current GT licence.

- 5.481. During the implementation of the Gas Act 1995, the DTI took the view that customers connected to independent systems that were supplied with LNG and LPG should not be denied the advantages of competition. As a result, Special Condition 18 is a condition that was included in Transco plc's GT licence, on 1 March 1996, at the DTI's behest.
- 5.482. There are five independent LNG networks in Scotland and four independent LPG networks (in Scotland, Wales and the North of England). All of these networks were independent networks when Special Condition 18 was introduced (i.e. separate from the main UK gas transportation system), and all of these systems bar one remain independent.
- 5.483. Under the provisions of Special Condition 18, customers connected to independent networks should be charged an average price for conveyance which is 'no more than the average charge for conveyance to premises in Great Britain'. In the case of the LPG networks, Transco is required to subsidise the cost of the gas itself, as well as the costs of conveyance.
- 5.484. The DTI will be issuing a position paper in due course to inform the industry how it proposes to take this matter forward. However, the Department wishes to notify all relevant parties that this review is taking place and would welcome comments from respondents on this issue.
- 5.485. Following the outcome of the DTI's review of the provisions of Special Condition 18, any changes necessary to Transco's licences will be implemented as part of the formal Section 8AA consultation.

Special Condition 19 – Emergency Services to or on Behalf of Another Gas Transporter

Description

- 5.486. This condition provides that the Authority can direct, following consultation with the HSE, for the licensee to offer terms to enter into an agreement with other gas transporters for the provision of emergency services where a major loss of supply has occurred. Such agreement may provide for the licensee to recover all costs reasonably related to the emergency service provision, a reasonable commercial profit and appropriate indemnities against third party claims.

September document

5.487. In the informal licence consultation, Ofgem considered that this licence condition should apply to all NTS and DN-GTs and proposed that it should be included in all NTS and DN-GT licences as a standard special condition.

Respondents' views

5.488. The provision of emergency services is a key area of concern for IGTs. Responses in relation to the following general issues and the associated implications are discussed in Chapter 4 earlier in this document:

- ◆ emergencies at DN boundaries;
- ◆ emergency services provision to IGTs; and
- ◆ emergency service provision from the DNs to the NTS.

5.489. All seventeen respondents responded to this issue. One potential purchaser agreed to this condition in its current form and one shipper/supplier stated the proposal seemed reasonable. Another potential purchaser agreed to the condition in its current form but stated that it would prefer it to include 1st line emergency response.

5.490. Six respondents, four shipper/suppliers, one IGT and one potential purchaser stated that the condition should be extended to monopoly emergency services.

5.491. Three shipper/suppliers, one IGT, one respondent and GISG stated that the condition should include all emergency services and repair and restoration services.

5.492. One respondent stated that 'major loss of supply' needs to be defined to ensure that all DNs have comfort in what a 'major loss of supply' is

5.493. NGT stated that there should be a condition requiring first line emergency responses for each DN. NGT stated that DNs should continue to provide IGT services under existing commercial contracts.

5.494. One respondent also supported the proposal for Transco to make available a 5km strip of records to emergency staff on site, for adjoining networks. This

respondent also held the opinion that current pipeline security standards should continue to apply within all NTS and DN-GT licences.

5.495. Energywatch stated that the coordination of emergency services and the restoration of supply will be a critical success factor for the new regime and that any significant differences in the arrangements for handling emergencies would jeopardise safety and customer service.

5.496. This condition has been presented to DISG members. One IGT sought clarification regarding the definition of a major loss of supply.

Ofgem's views

5.497. Ofgem acknowledges the strength of responses to the more general emergency services related issues raised. These are addressed earlier in this document in Chapter 4. As we state in Chapter 4, Ofgem does not believe that this condition should be expanded at this time to cover emergency services between gas transporters other than when a major loss of supply has occurred.

5.498. Given the specific views expressed by respondents on Special Condition 19, Ofgem is minded to include this licence condition in all NTS and DN-GT licences. However, this Special Condition refers to the LNG storage business. Given the decision that LNG storage businesses should only apply to the NTS, Ofgem is of the view that this licence condition should become a standard special condition applicable to all DN-GTs (excluding LNG storage references).

5.499. Ofgem notes the concerns expressed by respondents regarding the definition of a "major loss of supply" but does not consider that such issues are within the scope of the DN sales process. Ofgem would welcome further views from respondents in this regard.

5.500. The proposed drafting for this Condition (Standard Special Condition A41) is provided for comment in Appendix 7B.

5.501. As discussed in Chapter 4, to address the issue of LNG, a new NTS Special Condition has been introduced to "augment" this standard special condition with LNG related provisions (Special Condition C1, paragraph 13). This is discussed in further detail in Chapter 6.

5.502. Ofgem invites respondents' views on its proposals for Special Condition 19. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 23 – Provision of Meter and Meter Reading Services

Description

5.503. This condition requires Transco to make available the terms on which it shall provide metering services direct to the relevant supplier. It was amended in Transco's licence as part of Ofgem's RGMA reforms so that it applies to the provision of services to suppliers and not (as was previously the case) shippers. This modification will help to ensure that where it becomes evident that changes to the RGMA Baseline are necessary to reflect the development of the gas metering market, these cannot be unreasonably refused by Transco.

5.504. Except in so far as the Authority agrees, the licensee shall enter into agreements with the supplier for:

- ◆ gas meters;
- ◆ metering services other than provision of gas meters (i.e. services relating to the operation of the meter); or
- ◆ meter reading services.

September document

5.505. Ofgem set out, as part of the informal licence consultation that the Special Condition contained in Transco's licence should become a standard special condition applicable to all licences.

Respondents' views

5.506. One shipper supported the retention of this condition within all NTS and DN-GT licences.

5.507. In contrast, a potential purchaser considered that this condition should not apply to IDNs and should only be applicable within the licence of the NTS and RDN-GTs. This potential purchaser stated that, in the event that IDNs are required to comply with this condition, they should receive a derogation from the obligation to publish a schedule of charges in relation to their meter reading activities, in view of the fact that NGT has already received a derogation of this nature.

Ofgem's proposals

5.508. Ofgem remains of the view that this Special Condition should become a standard special condition applicable to all NTS and DN-GTs. The proposed drafting for this Condition (Standard Special Condition A43) is provided for comment in Appendix 7B.

5.509. Ofgem invites respondents' views on its proposals for Special Condition 23. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 25A – Assignment of Licence

Description

5.510. Special Condition 25A requires that the licensee may only transfer its licence (either in whole or in relation to part of an authorised area or any specified pipeline system) if it:

- ◆ complies with the procedure in Section 8AA of the Gas Act; and
- ◆ obtains the prior written consent of the Secretary of State.

September document

5.511. Ofgem proposed, as part of the September licence consultation, that this condition should become a standard special condition contained in all NTS and DN-GT licences.

Respondents' views

5.512. Ofgem did not receive any comments in relation to this proposal.

Ofgem's proposals

5.513. Ofgem remains of the view that this Special Condition should become a standard special condition contained in all NTS and DN-GT licences. The proposed drafting for this Condition (Standard Special Condition 45) is provided for comment in Appendix 7B.

5.514. Ofgem invites respondents' views on its proposals for Special Condition 25A. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 26 – Prohibited procurement activities

Description

5.515. This condition requires that the licensee shall not enter into or otherwise acquire transportation commodities, gas or gas derivatives with the intention of selling, assigning or disposing of such assets to third parties without the consent of the Authority.

5.516. The prohibition does not apply where the purchase or acquisition occurs for the purposes of facilitating balancing management or constraint management, so long as the transaction is conducted on economic and efficient terms and facilitates economic and efficient operation of the transportation system.

September document

5.517. In the informal licence consultation Ofgem proposed that, in light of the conclusions set out in the Roles & Responsibilities decision document⁴⁰, the current Special Condition 26 should be split as follows:

- ◆ **A Special Condition should be placed in the NTS–GT licence:** allowing the purchase of gas or gas derivatives to facilitate balancing management where the transaction is conducted on economic and efficient terms and contributes to the economic and efficient operation of its system; and
- ◆ **A Standard Special Condition is placed in the NTS and DN–GT licences:** allowing the purchase of transportation commodities, gas or gas derivatives for the purpose of facilitating constraint management where the transaction is conducted on economic and efficient terms and facilitates the economic and efficient operation of its system.

5.518. Ofgem additionally considered that the definitions in the condition would need to be carefully reviewed to ensure that they support the split in the roles and responsibilities between the NTS and DNs in the event of any DN Sale.

Respondents' views

5.519. Six respondents commented on the proposals regarding Special Condition 26.

5.520. Of these, three potential purchasers, a shipper/supplier and NGT expressed broad support for Ofgem's proposal to include a standard special condition within the licences of all GTs in relation to the purchase of transportation commodities to facilitate constraint management. The shipper/supplier was of the opinion that it would be necessary to carefully control the DNs to prevent them from destabilising the arrangements while a potential purchaser highlighted that the drafting should allow the appropriate arrangements to be made in relation to the system management. NGT also clarified that further consideration of these obligations would need to be undertaken to ensure that they are compliant with the exit arrangements as these develop further.

⁴⁰ *National Grid Transco – potential sale of gas distribution network businesses, Allocation of roles and responsibilities between transmission and distribution networks, Ofgem, April 2004*

- 5.521. Two potential purchasers and NGT considered that the NTS licence condition should be retained in its current form and that, as such, it should cover balancing management and constraint management services. In this respect, they supported the proposal to incorporate an additional Special condition to be placed on the NTS. A shipper/supplier considered that conditions in this regard, would need to be drafted to allow the NTS to retain overall supply demand system balance and system balance action relating to localised constraint management.
- 5.522. However, one potential purchaser, had concerns that, as proposed, the licences would treat existing Special Condition 26 and Special Condition 27 inconsistently. In particular, this respondent highlighted that the provisions of Special Condition 26 would be contained in a Standard Special Licence Condition applicable to the NTS and DN-GTs with an additional NTS Special Condition that would accommodate NTS-specific conditions. In comparison, the provisions of Special Condition 27 would be contained within respective NTS and DN-GT Special Conditions. The purchaser therefore had concerns that the way in which the conditions incorporating Special Condition 26 would work together may cause confusion and, in addition, may not replicate the provisions that the existing condition contains.
- 5.523. One shipper/supplier stated that more careful drafting in relation to this condition would need to be undertaken to ensure that all relevant activities are retained as permitted activities.
- 5.524. In relation to the drafting of the licence conditions presented to DISG members, a potential purchaser highlighted that “Transportation system” should be a defined term within this standard special condition and that an amendment to the definition of “Capacity rights” should be made to include the words “where applicable”.

Ofgem’s proposals

- 5.525. Following consideration of respondents’ views, Ofgem has altered its view on how the conditions within the current Special Condition 26 should be divided between the NTS and the DNs. Ofgem considers that it would be most appropriate for:

- ◆ a Special Condition to be placed on the NTS–GT licence in relation to its role as energy balancer for the entire network, procurement of gas for shrinkage on the NTS, and constraint management services; and
- ◆ a standard special condition to be placed on the DN–GT licences only, in relation to shrinkage procurement (for gas lost on that DN) and constraint management services.

5.526. Ofgem notes that this change in its view (in that the NTS would not be subject to a standard special condition) is the result of wishing to make very clear to all parties the roles and responsibilities of the NTS and the DNs. By having a separate Special Condition applicable to all of Transco’s NTS activities, Ofgem believes that the clarity of Transco’s role as energy balancer for the entire network is best preserved.

5.527. The proposed drafting for these Conditions (Special Condition C4 and Standard Special Condition D4) is provided for comment in Appendix 7B.

5.528. Ofgem invites respondents’ views on its proposals for Special Condition 26. Following consideration of respondents’ views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 27 – Licensee’s procurement and use of system management services

Description

5.529. This condition requires the licensee to operate the NTS in an efficient, economic and co-ordinated manner and prohibits undue discrimination or undue preference in procurement or use of system management services. It also places reporting obligations to the Authority on the licensee.

September document

5.530. In the informal licence consultation, Ofgem proposed that this condition would need to be divided to reflect the treatment of constraint management and balancing in Special Condition 26. As such Ofgem's initial proposal was that:

- ◆ a Special Condition should be placed in the NTS-GT licence to operate its system in an efficient, economic and co-ordinated manner and to prohibit undue discrimination;
- ◆ a standard special condition should be placed in DN-GT licences to operate DNs in an efficient, economic and co-ordinated manner and to prohibit undue discrimination; and
- ◆ a further standard special condition may be required to oblige licensees not to prejudice each others' systems.

Respondents' views

5.531. Two shipper/suppliers, an IGT and a potential purchaser expressed support for the proposal to include conditions which would prohibit the NTS and DN GTs from prejudicing the operation of each others' systems. One shipper/supplier clarified that this provision should be extended to include IGTs as well as the NTS, DN GTs while the other shipper/supplier considered that it would be appropriate to include a more specific provision which would provide greater practical guidance and safeguards.

5.532. NGT considered that the current conditions in the NTS-GT licence should be retained but that, with respect to the DN GT licence condition a condensed version should be developed to reflect more accurately the services that they would provide. In a similar respect, a potential purchaser highlighted that as the existing condition relates primarily to NTS activities, the obligations that have been proposed in relation to DN-GTs would be too onerous. This respondent also queried whether this should be a standard special condition.

5.533. A potential purchaser also queried how such a provision would operate in practice at the DN level.

Ofgem's proposals

- 5.534. Following consideration of respondents' views, Ofgem has retained its view that separate licence conditions (a Special Condition in the NTS-GT licence and a standard special condition in DN-GT licences) should be put in place obliging licensees to operate their system in an efficient, economic and co-ordinated manner and prohibiting undue discrimination. Ofgem agrees with Transco's view that the standard special condition in DN-GT licences should be narrower in scope than that applied to the NTS. As such, Ofgem proposes that a narrower definition of "system management services" is applied to the DNs than the NTS. Therefore:
- ◆ in the NTS Special Condition system management services are defined to include balancing of the NTS, including balancing trades, as well as constraint management; whereas
 - ◆ in the DN-GT standard special condition, system management services are defined to include procurement of gas to replace that lost in the licensee's pipeline system and constraint management only. Given that DNs will not be responsible for energy balancing, the provisions relating to the costs and volumes of system management services that are used on the Network Code are omitted in the DN-GT licences.
- 5.535. Ofgem considers that it is not within the scope of the DN Sales process to extend this condition to cover IGTs.
- 5.536. The proposed drafting for these Conditions (Special Condition C5 and Standard Special Condition D5) is provided for comment in Appendix 7B.
- 5.537. Proposals for a new licence condition which requires GTs not to prejudice each others' systems is discussed in Chapter 6 (Standard Special Condition A17).
- 5.538. Paragraph 2 of the proposed Special Condition C5 and Standard Special Condition D5 sets out that the "licensee shall neither unduly discriminate nor unduly prefer in its procurement or use of system management services as between any persons or classes of persons". As Transco plc will retain its NTS and DN businesses within a single legal entity, each business will be an internal business unit of a single company and therefore may not be subject to the

provisions of paragraph 2 as drafted. It may therefore be necessary to amend these conditions so that Transco's NTS business is also prevented from unduly discriminating in favour of the Transco RDN business units and vice versa. Ofgem intends to discuss this matter further at an upcoming DISG meeting.

- 5.539. Ofgem invites respondents' views on its proposals for Special Condition 27. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 28A – Revenue restriction definitions

Description

- 5.540. This condition defines a number of terms in the revenue restrictions.

September document

- 5.541. In the informal licence consultation Ofgem proposed that this condition should be amended and split into Special Conditions setting out the definitions which are relevant for each DN licence and the NTS licence. As such, it proposed to split this condition into Special Conditions for NTS and DN-GT licensees.

Respondents' views

- 5.542. Ofgem did not receive any comments in relation to this proposal.

Ofgem's proposals

- 5.543. As set out in Chapter 3 of this document, Ofgem is publishing a formal section 23 notice of its intention to change this condition for the purposes of separating the price controls between Transco's NTS and each of its DNs.
- 5.544. It will be necessary to change further this condition to:

- ◆ ensure that the use of the term “shipper” within the NTS Special condition is appropriate given Option 2A for offtake arrangements;
- ◆ ensure enable the revenue adjustments required in respect of DN GTs for the purposes of Option 2A for offtake arrangements;
- ◆ develop incentives on NTS and DN-GTs to support the NTS offtake arrangements;
- ◆ introduce a “safety net” to ensure that customers are protected in the event that costs exceed benefits and retained until the end of the process; and
- ◆ develop proposals that are robust to the separation of the networks from Transco plc.

5.545. The proposed new Special Conditions that will be introduced pursuant to the formal section 23 notice (subject to respondents’ views) will therefore need substantial amendment at the section 8AA notice stage. The drafting to reflect these changes is not attached in the draft licences set out in Appendix 7B of this document. Ofgem will be publishing this drafting in the near future and it will be discussed at an upcoming DISG meeting. The view of respondents’ set out above will be considered as part of this process

5.546. Ofgem invites respondents’ views on its proposals for Special Condition 28A. Following consideration of respondents’ views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 28B – Restriction of revenue in respect of the NTS Transportation Owner Activity, Distribution Owner Activity and NTS System Operation Activity.

Description

5.547. This condition defines the price controls and incentives applicable to Transco.

September document

5.548. In the informal licence consultation Ofgem proposed to divide this condition into Special Conditions for NTS and DN-GTs setting out the price controls and incentives relevant to each entity. Ofgem also considered that it might be necessary to reflect any necessary changes to the price control treatment of shrinkage arrangements.

Respondents' views

5.549. One potential purchaser commented on this issue, as well as NGT. The potential purchaser considered that Ofgem would need to ensure that the NTS incentive scheme did not include provisions regarding DN-GTs and that correspondingly, a DN incentive scheme would need to be developed to allow an understanding of the regulatory risk involved.

5.550. The potential purchaser perceived that, in relation to the treatment of shrinkage within the price control, further clarification would be required, while in contrast, NGT was of the opinion that it would not be appropriate for the shrinkage provisions to be amended as a result of a DN sale.

5.551. The potential purchaser had some more specific concerns regarding the drafting of the price control licence conditions proposed within the draft Section 23 notice. As an overall concern, this respondent considered that it would be important for Ofgem to ensure that the price control provisions are adequately reflected within each of the DN licences.

5.552. The potential purchaser also highlighted that it was unsure how the term “prescribed rates” would operate within the DN Special Condition regarding the Restriction of Revenue in respect of the Distribution Network Transportation Activity. In particular, they had concerns that if separate rating assessments were

not undertaken where a company were to own more than one DN, the ratings would need to be split within the DNs and that, as drafted, provisions for ratings to be split are only made if NGT were to continue to hold all of the DNs and the NTS. In addition, this potential purchaser was unsure as to how prescribed rates would be allocated to each of the independent DNs.

5.553. This condition was also presented to DISG members. Following this, Ofgem received a number of comments regarding the development of an incentive scheme.

5.554. A potential purchaser and two shipper/suppliers expressed support for the development and implementation of incentives to encourage efficient management of incentives. Two potential purchasers and two further shipper/suppliers also expressed interest in the separate incentives consultation that Ofgem has stated its commitment to producing.

5.555. One potential purchaser also considered that any incentive scheme should be kept as simple as possible in order that they are straightforward for participants to understand. In this regard, the potential purchaser also suggested that the incentive scheme should be developed as soon as possible in order that DNs are able to fully understand the associated regulatory risk.

Ofgem's proposals

5.556. As set out in Chapter 3 of this document, Ofgem is giving notice of its intention to modify this condition such that separate Special Conditions apply to each DN and NTS licensee. These Special Conditions will ensure that the separate price controls apply to each of the individual DNs and the NTS through licensing arrangements⁴¹.

5.557. As explained in relation to Special Condition 28A, a number of further modifications to this condition are envisaged.

⁴¹ Independently of the DN Sales consultation process, Ofgem published a separate notice on its decision to change paragraph 14(11) of this condition at the same time as the Section 23 notice accompanying this document was published. If the changes to paragraph 14(11) are made, these will need to be reflected in the licence conditions being modified for the Section 8AA consent (and associated Section 23 notice).

5.558. The proposed new Special Conditions that will be introduced pursuant to the formal section 23 notice (subject to respondents' views) will therefore need substantial amendment at the section 8AA notice stage. The drafting to reflect these changes is not attached in the draft licences set out in Appendix 7B of this document. Ofgem will be publishing this drafting in the near future and it will be discussed at an upcoming DISG meeting. The points raised by respondents as set out above will be considered as part of this process.

5.559. Ofgem invites respondents' views on its proposals for Special Condition 28B. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 29 – Allocation of revenues and costs for calculation under price control

Description

5.560. This condition sets out the licensee's obligations regarding the allocation or attribution of revenues, costs, assets and liabilities by the licensee in order to calculate values referred to in Special Condition 28B.

September document

5.561. As part of the informal licence consultation, Ofgem detailed that this condition would need to be tailored to reflect the activities conducted by each licensee. Ofgem considered that the provisions of this condition should be contained in a Special Condition for each licensee, linked to the revenue restriction condition.

Respondents' views

5.562. Ofgem did not receive any comments in relation to this proposal.

Ofgem's proposals

- 5.563. Ofgem still considers that the provisions of this condition should be contained in a Special Condition for each licensee, linked to the revenue restriction condition and amended to reflect the relevant activities of each licensee.
- 5.564. The proposed drafting for these Conditions (Special Condition C9 and Special Condition E3) is provided for comment in Appendix 7B.
- 5.565. Ofgem invites respondents' views on its proposals for Special Condition 29. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 30 - Supplementary provisions of the revenue restrictions

Description

- 5.566. This condition sets out activities that can be treated as excluded services and defines charges or proportions of charges which can be treated as excluded revenue. These include last resort payment claims, supplemental charges, emergency service charges, charges relating to gas illegally taken or works at connection points.

September document

- 5.567. In the informal licence consultation Ofgem considered that the provisions of this condition should be contained in a Special Condition for each licensee, linked to the revenue restriction condition and amended to reflect the relevant activities of each licensee.

Respondents' views

- 5.568. NGT expressed support for Ofgem's proposal that the provisions contained in this condition should be retained within both the NTS and DN-GT licences and noted that the licence obligation would need to be amended to reflect any decision regarding LNG storage in relation to the NTS.
- 5.569. In addition, a potential purchaser considered that IDNs that also own metering businesses should be obliged to prepare separate Regulatory Accounts under the provisions of this condition for both metering and meter reading services.

Ofgem's proposals

- 5.570. Ofgem considers that the provisions of this condition should be contained in a Special Condition for each licensee, linked to the revenue restriction condition and amended to reflect the relevant activities of each licensee. The proposed drafting for these Conditions (Special Condition C10 and Special Condition E4) is provided for comment in Appendix 7B.
- 5.571. Ofgem invites respondents' views on its proposals for Special Condition 30. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 31 – Restriction of prices in respect of tariff capped metering activities

Description

- 5.572. This condition sets tariff caps for metering activities which can be increased in line with the Retail Prices Index, with a claw back for 2005, and specifies the maximum, indexed tariff cap values for charges for different metering activities.

September document

- 5.573. Ofgem proposed, as part of the informal licence consultation, to introduce a standard special condition within all NTS and DN-GT licences. As such, both the NTS and DN-GTs would be required to comply with the conditions contained in its price control which relate to the provision of metering services.
- 5.574. Ofgem also detailed that further consideration would need to be given to the apportionment of the tariff cap.

Respondents' views

- 5.575. A shipper/supplier was of the opinion that tariff caps should be applied informally across IDNs and RDNs while, in contrast, one potential purchaser considered that IDN-GTs should not have a regulated metering obligation. This respondent was therefore of the opinion that the price control arrangements should only be incorporated within RDN-GT Special conditions.

Ofgem's proposals

- 5.576. After further consideration, Ofgem believes that the provisions of Special Condition 31, should be included within Special Conditions for each licensee. This is consistent with the treatment of the other key price control related conditions. However, as part of the DN sales project, it is not considered appropriate to change the provisions of Special Condition 31, and as such, the provisions included within these Special Conditions are the same for all NTS and DN-GTs. In Ofgem's view it is not appropriate to differentiate between RDN and IDN-GTs with respect to regulated metering obligations.
- 5.577. The proposed drafting for these Conditions (Special Condition C12 and Special Condition E5) is provided for comment in Appendix 7B.
- 5.578. Ofgem invites respondents' views on its proposals for Special Condition 31. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be

published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 32 – Non-discrimination in the provision of metering activities

Description

- 5.579. This condition requires the avoidance of undue discrimination in the provision of metering activities.

September document

- 5.580. In its informal licence consultation Ofgem proposed that this condition should be included as a standard special condition in all NTS and DN-GT licences.

Respondents' views

- 5.581. One shipper/supplier stated that IDN purchasers who own a metering business should be bound by the non-discrimination provisions included within this condition.
- 5.582. A further potential purchaser stated that IDN GTs should not have a regulated metering obligation and, as such, considered that the price control arrangements should only be incorporated within RDN-GT Special conditions..
- 5.583. This condition was presented to DISG members. Concern was expressed by participants regarding the potential for fragmentation of metering services. One potential purchaser also highlighted that this may be accentuated by the fact that quantum meters are not capable of managing a range of different changes.

Ofgem's proposals

- 5.584. Ofgem considers that it is inappropriate to differentiate between RDN and IDN-GTs with respect to regulated metering obligations and therefore that they should be subject to the non-discrimination obligations contained in this condition. As such, Ofgem remains of the view that this condition should be included as a standard special condition in all NTS and DN-GT licences. The

proposed drafting for this Condition (Standard Special Condition A46) is provided for comment in Appendix 7B.

- 5.585. Ofgem invites respondents' views on its proposals for Special Condition 32. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 33 – Information to be provided to the Authority in connection with the transportation system revenue restriction

Description

- 5.586. This condition requires the licensee to provide information statements to the Authority in connection with its transportation system revenue restriction.

September document

- 5.587. In the initial consultation document, Ofgem suggested that the provisions contained in this condition would need to be split appropriately between the NTS and DN GT's licence conditions, and amended to provide separate tables for each DN with appropriate adjustments to the references to the price controls. As such, Ofgem suggested that the condition should be separated into Special Conditions for each NTS and DN-GT licence.

Respondents' views

- 5.588. Whilst Ofgem did not receive any views relating specifically to this condition, several respondents expressed support for the provision of separate accounts for each individual distribution network to ensure the equivalent treatment of IDN and RDN businesses.

Ofgem's proposals

5.589. Ofgem remains of the view that this condition should be split appropriately for the NTS and DN-GTs' licence conditions, and amended to provide separate tables for each DN with appropriate adjustments to references to the price controls. Therefore, this condition should be separated into Special Conditions for each NTS and DN-GT licence.

5.590. In the draft licences:

- ◆ Special Condition C14 sets out the NTS GT's reporting obligations in this regard; and
- ◆ Special Condition E6 sets out the DN-GTs' respective obligations.

5.591. The proposed drafting for these Conditions is provided for comment in Appendix 7B.

5.592. Ofgem invites respondents' views on its proposals for Special Condition 33. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 34 – Licensee's methodology for determining incremental entry capacity volumes

Description

5.593. This condition requires licensees to prepare and submit each year an audited incremental entry capacity release methodology statement setting out the methodology by which it will determine whether to make incremental entry capacity available for sale to shippers.

September document

- 5.594. In its informal licence consultation Ofgem proposed that, as the provisions contained within this condition related only to the NTS, this condition should be retained as a Special Condition in the licence of Transco's NTS GT only. Ofgem also noted that a corresponding provision would be required for NTS exit capacity volume.

Respondents' views

- 5.595. Whilst one potential purchaser supported the proposal that this condition should only apply to the NTS, a shipper/supplier raised the issue that there was a potential for DN entry points for gas and therefore that perhaps this condition should also apply to DN GTs. Similarly, the potential purchaser also requested clarification regarding the impact of this condition on DN entry points and the way in which the NTS and DNs would interact in this respect.

Ofgem's proposals

- 5.596. Ofgem recognises the point raised by a shipper/supplier, relating to DN entry points. We do not consider it appropriate to amend Ofgem's proposals relating to this condition at this stage as there are no significant DN entry points at this time. This issue is being considered through the DISG.
- 5.597. Special Condition C15 sets out the NTS's obligations in this regard.
- 5.598. Ofgem invites respondents' views on its proposals for Special Condition 34. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 35 – NTS performance reporting

Description

- 5.599. This Special Condition provides for the collection of information by the licensee to an appropriate degree of accuracy, to monitor the environmental performance of the NTS and facilitate the development of an expenditure monitoring framework.

September document

- 5.600. As part of the informal licence consultation, Ofgem detailed that it was minded to maintain this condition as a Special Condition within the licence of the NTS operator.

Respondents' views

- 5.601. Ofgem did not receive any views relating to this licence condition.

Ofgem's proposals

- 5.602. Ofgem remains of the view that this condition should be retained as a Special Condition in the licence of the NTS operator only (Special Condition C16). The drafting for this condition is set out in Appendix 7B.
- 5.603. Ofgem invites respondents' views on its proposals for Special Condition 35. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 36 – LDZ incentive scheme and performance reporting

Description

- 5.604. This condition defines the incentive and performance measures applicable to Transco's LDZ network.

September document

- 5.605. In its informal licence consultation Ofgem proposed to maintain this condition as a Special Condition contained in DN licences.

Respondents' views

- 5.606. Ofgem did not receive any views specifically relating to this licence condition. However, energywatch stated that Ofgem should ensure that information on service performance is collected and published.

Ofgem's proposals

- 5.607. Ofgem remains of the view that this condition should be retained as a standard special condition in DN licences. As discussed in Chapter 4, since publication of the September document, Ofgem has discussed at DISG the proposal to extend the provisions of this condition to oblige DN-GTs to conduct customer satisfaction surveys. NGT currently undertakes such surveys as part of its internal processes. Hence, placing this obligation on DN-GTs would allow for the formalisation of current practice and ensure its continued provision despite different ownership of some of the DNs.
- 5.608. Views are invited as to whether it is appropriate to place this obligation on DNs. Views are also invited on the number of questions that is appropriate to be included in the survey and on the frequency of such a survey.
- 5.609. The proposed drafting for this Condition (Standard Special Condition D9 Distribution Network transportation activity incentive scheme and performance reporting) is provided for comment in Appendix 7B.

5.610. Ofgem invites respondents' views on its proposals for Special Condition 36. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 37 – Exit code statement

Description

5.611. This condition requires the annual preparation and submission of an exit code, which provides a description of the services provided and revenue received by the licensee's NTS activity and DN activity.

September document

5.612. Ofgem set out its expectation, within the informal licence consultation, that this condition would change with the introduction of the UNC/Oftake Code and that it would require amendment to reflect activities conducted by the separate licensees. Ofgem proposed maintaining this condition as a Special Condition for each licensee to reflect their respective responsibilities.

Respondents' views

5.613. NGT considered that this condition would no longer seem appropriate given the introduction of NTS exit arrangements.

Ofgem's proposals

5.614. Ofgem has given further consideration to this condition. The condition seeks to achieve clarity in the services and revenues shared between the NTS and DN activities. Ofgem considers that this condition will be redundant given other changes in the licence. Ofgem therefore expects that this condition will be switched off when the sale process is complete. However, to allow for the possibility of future divergence in requirements for this Condition, Ofgem

proposes that this Condition will be replaced with a standard special condition in the licences of all DN licensees and a Special Condition for the NTS licensee.

5.615. The proposed drafting for these Conditions (Special Condition C17 and Special Condition D7) is provided for comment in Appendix 7B.

5.616. Ofgem invites respondents' views on its proposals for Special Condition 37. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 38 – Restriction on Use of Information deriving from the EnMo Business

Description

5.617. This licence condition required the licensee to procure an undertaking relating to the disclosure of confidential information to EnMo.

September document

5.618. Ofgem considered as part of its informal licence consultation that this provision would no longer be required as the EnMo business has been disposed of by NGT. As such, Ofgem proposed to delete this condition.

Respondents' views

5.619. This proposal was presented at a DISG meeting where DISG participants expressed support for the removal of this licence condition.

Ofgem's proposals

5.620. Having considered respondents' views, Ofgem continues to believe that it is appropriate to remove this licence condition.

5.621. Ofgem invites respondents' views on its proposals for Special Condition 38. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Special Condition 39 – Charging of Gas Shippers – Domestic Infill Premises

Description

5.622. This Condition relates to the charges that a licensee may charge where the licensee has, on request, extended a gas main to specifically connect premises.

September document

5.623. In the September licence consultation Ofgem proposed that this condition should apply to both NTS and DN-GT Licences as a standard special condition.

Respondents' views

5.624. A potential purchaser questioned whether Special Condition 39 would be better suited as a Special Condition (rather than a Standard Special) as it relates to charging and, potentially, a network owner's revenue.

Ofgem's proposals

5.625. Ofgem remains of the view that this condition should apply to both NTS and DN-GT Licences as a standard special condition, as it will not vary across licensees. The proposed drafting for this Condition (Standard Special Condition A47) is provided for comment in Appendix 7B.

5.626. Ofgem invites respondents' views on its proposals for Special Condition 39. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales

then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Schedules to Transco's GT licences

Description

5.627. There are a number of schedules to Transco's GT licence which set out, among other things, the output measures for the NTS price control, Transco's Authorised Area, and the circumstances in which the Authority may revoke Transco's GT licence.

September document

5.628. In the informal licence consultation Ofgem noted that:

- ◆ Schedule A – NTS output measures for the price control: Ofgem noted that this schedule may need to be revised subject to reform of the interruptions and exit capacity arrangements.
- ◆ Schedule 1 – Specified Area: Ofgem noted that this issue was under consideration as part of the licence application consultation process.
- ◆ Schedule 2 – Revocation of Licence: Ofgem does not propose to modify this schedule
- ◆ Schedule 3 – Transportation Services Area: Ofgem noted that this issue was under consideration.

Respondents' views

5.629. Ofgem did not receive any comments in relation to these schedules, except insofar as Ofgem received views on the authorised areas to be granted to DN-GTs as a part of its grant of licence consultation.

Ofgem's proposals

5.630. Ofgem's proposals with respect to each of the schedules are as follows:

- ◆ Schedule A – NTS output measures for the price control: this schedule may need to be revised subject to reform of the interruptions and exit capacity arrangements;
- ◆ Schedule 1 – Specified Area: this schedule will remain unchanged with the specified area being the whole of Great Britain;
- ◆ Schedule 2 – Revocation of Licence: this schedule does not require modification;
- ◆ Schedule 3 – Transportation Services Area: this schedule will remain unchanged with the specified area being the whole of Great Britain.

5.631. Ofgem invites respondents' views on its proposals for the Schedules to Transco plc's licences. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be consulted upon in February 2005. Further consultation may take place during this period through the DISG meetings.

6. New licence conditions

6.1. In September 2004 Ofgem published for consultation its initial thoughts on the restructuring of Transco's original GT licence and the five new additional GT licences⁴². Ofgem considered that it may be appropriate to introduce certain new obligations that are not covered by Transco's original GT licence and the five new additional GT licences in the form required. Ofgem invited views on a number of possible new NTS and DN GT licence conditions that could be adopted as part of the DN sales reforms. Following consideration of respondents' views and further consideration of the key provisions required, Ofgem is proposing to introduce new licence conditions relating to:

- ◆ the private CLM procedure;
- ◆ the switch on/off of standard conditions and standard special conditions;
- ◆ implementation of gateway requirements in relation to:
 - ◆ DN interruption reform; and
 - ◆ Agency obligations;
- ◆ independence of market for balancing;
- ◆ requirement not to prejudice the systems of other GTs;
- ◆ inter-operator service agreements:
 - ◆ adjustments to de minimis business cap to take account of SOMSAs; and
 - ◆ first line emergency response services to the NTS;
- ◆ joint office governance arrangements;
- ◆ connections;

⁴² *National Grid Transco – Potential sale of gas distribution network businesses. Initial thoughts on restructuring of Transco plc's Gas Transporter Licences. Ofgem, September 2004*

- ◆ governance of technical standards;
 - ◆ arrangements for gas measurement;
 - ◆ business separation;
 - ◆ separation of monopoly and competitive activities for those DNs acquired by a group with competitive gas activities;
 - ◆ structural separation of the NTS and RDNs within Transco plc to largely replicate the impact of legal separation; and
 - ◆ treatment of LNG Storage.
- 6.2. The Authority reserves the right to propose additional new licence conditions during the Section 8AA process (and associated additional Section 23 notice), as part of the consents to the disposal of DN assets or at a later stage in the process.
- 6.3. This chapter provides:
- ◆ a brief description of each of the new licence conditions proposed;
 - ◆ a high level view of the proposed treatment for each new condition as set out in the September document;
 - ◆ a summary of the responses received in relation to each of the proposed new licence conditions; and
 - ◆ a description of Ofgem's views and associated decisions regarding each of the proposed new licence conditions.

Private CLM procedure

September Document

- 6.4. As discussed in Chapter 4, in the September document Ofgem outlined its proposals regarding the introduction of a private CLM procedure, which is intended to be equivalent to the statutory CLM procedure except that it would apply only to the class of NTS and DN-GT licensees.

6.5. Following the publication of the September document, in October 2004 Ofgem published initial drafting of the private CLM procedure⁴³ for consultation. In this document, Ofgem indicated that it intended to replicate the thresholds that apply in respect of the statutory CLM process within the private CLM process. As such, under the private CLM procedure, relevant licence holders would be able to prevent the Authority from directing a modification where either of the following two tests are met:

- ◆ the objecting licence holders constitute at least 20% of relevant licence holders; or
- ◆ the objecting relevant licence holders account for at least 20% of market share⁴⁴.

Respondents' views

6.6. A high-level summary of respondents' views with respect to the principle of implementing a private CLM procedure was provided in Chapter 4, along with Ofgem's proposals in the light of these views. However, a number of respondents commented on the detail of the private CLM drafting provided. These comments are set out below.

6.7. Three potential purchasers and NGT commented on the proposed thresholds necessary to veto the approval of a licence modification under the private CLM process.

6.8. NGT and SSE considered that the 20% threshold to block any proposed modification should be retained, consistent with the statutory CLM procedure, especially in view of the extensive consultation that was carried out on this matter with respect to the statutory CLM procedure. Both respondents were also of the opinion that the 20% threshold should be calculated on the basis of the quantity of gas transported by the GT and that a second test should be carried out based on the number of relevant licences that the GT holds.

⁴³ *Ofgem initial drafting of private CLM licence condition*. Ofgem, October 2004

⁴⁴ Market share is calculated with reference to the total quantity of gas conveyed to the premises of consumers by the relevant licence holder.

- 6.9. In contrast, Macquarie (MGN) and United Utilities (UU) expressed concerns regarding the retention of the 20% threshold in a post-DN sales environment. In responses to the informal licence consultation and the draft Section 23 licence changes, MGN and UU highlighted that they considered that a framework of this nature could serve to discriminate against them as respective owners of a single DN. These two prospective buyers highlighted the need for all GTs to be treated equally under the provisions of the private CLM.
- 6.10. In particular, they set out that initially if a licence modification were proposed under the private CLM procedure, in relation to DN-GT licences both UU and MGN would retain the power of veto. However, they considered that if any further DNs were to be sold, UU and MGN would fall below the 20% threshold in terms of the number of licences and would therefore lose the power of veto. As such, MGN detailed that it would be content with the private CLM procedure as long as one NTS and four DN licences were granted.
- 6.11. Both MGN and UU were of the opinion that, if they were to purchase a DN business, they would have invested significant funds into a substantial entity and should therefore receive equal treatment with respect to the modification of their licence through the private CLM. As currently drafted they highlighted that SSE and NGT would have the power of veto available to them under a range of circumstances and that, as such, MGN and UU should also have this facility available to them.
- 6.12. MGN suggested that a short term solution could be that, in the event of common ownership of more than one licensee, all licences in such ownership should be counted as one for CLM voting purposes. MGN considered that it would be reasonable for any one party to be able to block a proposed licence modification, and stated that it would welcome CLM rules that would endure even if more DNs were sold by NGT and more licences were issued to present DN licensees. MGN also noted that under its proposals the market test would not be necessary. However, it considered that, if circumstances arose in which the market test would apply to gas network owners, consideration should be given to the fact that NGT has a dominant position and special steps may be necessary to create equity with other users.

- 6.13. One shipper/supplier suggested that, under the proposed private CLM procedure, any proposed licence amendment should be widely consulted upon to ensure that the views of all parties likely to be affected by the modification were taken into account. The shipper/supplier considered that this would be especially important in situations where it is clear that the change would have consequential effects on industry participants.
- 6.14. Some more specific comments were received from respondents regarding the proposed drafting of the condition.
- 6.15. SSE commented that the definition of “relevant licence holder” should be clarified to highlight that it would not be possible to introduce a standard special condition through the private CLM procedure and that the introduction of additional conditions could only be achieved through the attainment of individual consents. In addition, SSE considered that, in paragraph 6 it should be made clear that only the private CLM procedure would be applicable to modification of the standard special conditions, and that the statutory CLM would not be applicable in relation to these conditions.
- 6.16. In addition, SSE requested that Ofgem make clear the fact that the private CLM procedure would not be applicable to special licence conditions.
- 6.17. On a process point, UU set out that it would hope to see revised drafting in relation to the private CLM procedure prior to the Section 8AA consultation, while NGT asked for clarification regarding the timing of the proposed implementation of the private CLM procedure and specifically whether it would be introduced at the Section 23 or Section 8AA stage.

Ofgem’s proposals

- 6.18. In Chapter 4 Ofgem set out its proposals on the private CLM. In this section we set out our response and proposals on the specific drafting comments received.
- 6.19. Ofgem has considered the views of the prospective buyers and other respondents relating to the proposed voting thresholds within the private CLM. We recognise that the current drafting of the condition means that some GTs will maintain the individual ability to veto modification proposals. After careful consideration of these issues, Ofgem continues to propose that the voting

thresholds applied should be the same as those set out in the statutory CLM procedures. The private CLM is being proposed to mitigate the effects of the wholesale changes to Transco's licence on the workings of the statutory CLM procedure and to ensure that the level of flexibility afforded by the statutory CLM procedure is not negated as a result of any DN sales. As such, Ofgem considers that it is important that the threshold criteria within the private CLM mirrors that set out in the statutory CLM procedure. The statutory CLM procedure underwent substantial consultation before it was introduced and the different effects on licence holders were considered at this point. Ofgem welcomes respondents views.

- 6.20. Ofgem is proposing to introduce three new standard special conditions for the purposes of establishing the private CLM procedure to apply in respect of standard special conditions that apply to NTS and DN-GTs, as well as standard special conditions that apply only to NTS-GTs or DN-GTs separately. These are set out in Appendix 7B in Standard Special Condition A2 (Private Collective Modification Procedure in respect of standard special conditions applicable to both NTS and DN-GT licensees), Standard Special Condition B2 (Private Collective Licence Modification Procedure in respect of standard special conditions applicable to NTS licensees) and Standard Special Condition D2 (Private Collective Licence Modification Procedure in respect of standard special conditions applicable to all DN licensees).
- 6.21. Ofgem has considered the specific comments provided by respondents with respect to the drafting of this condition. However, Ofgem considers that the drafting consulted upon is sufficiently clear, and ensures consistency with the associated proposed switch on / switch off condition. Ofgem invites respondents to comment on the drafting in Appendix 7B.
- 6.22. Ofgem made it clear in the September document that its intention is, as far as practicable and appropriate, to replicate the existing structure of the GT licence as it exists today and to ensure consistency of modifications to ensure that Ofgem's regulatory control is not diminished as a result of the proposed transaction. Under the statutory CLM procedure, Ofgem can introduce (and has introduced) new standard conditions. In line with this, Ofgem is of the view that the private CLM procedure (which is intended largely to replicate the statutory

CLM procedure) should also enable the introduction of new standard special conditions which apply to NTS and DN-GTs or to NTS or DN-GTs separately.

- 6.23. The procedure can obviously not be used to introduce or modify special conditions that apply to individual GT licensees. Ofgem believes that the drafting of the proposed condition is sufficiently clear on this point.
- 6.24. Ofgem invites respondents' views on its proposals for these new licence conditions. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through DISG meetings in January 2005. If the Authority grants its consent to any DN sales then it is expected that these proposals (pursuant to a Section 8AA notice and an associated additional Section 23 notice) will be formally consulted upon in February 2005. Further consultation may take place during this period through the DISG meetings.

Switch on/switch off

September document

- 6.25. As discussed in Chapter 4, where a modification to a standard condition is required, Ofgem proposes to replicate the relevant standard condition as a standard special condition (incorporating the necessary modifications) which could be subject to the private CLM procedure. In order that the NTS and DN-GTs are not subject to two very similar conditions in respect of the same issue, Ofgem proposes to "switch off" those standard conditions that have been replaced by standard special conditions.
- 6.26. Ofgem proposed, pursuant to section 7(B)(7)(a) of the Gas Act, to introduce a new special condition enabling the Authority also to switch on or switch off standard conditions in sections A and B of the GT licence⁴⁵, with the consent of the licence holder. It is also proposed that such a condition could be used to switch on or off standard special conditions. As with Standard Condition 2, this

⁴⁵Section C of the Standard Conditions of the GT licence is already capable of being switched on or switched off under Standard Condition 2.

switch would be capable of being used in relation to entire conditions or parts of conditions and would not be time limited, enabling it to be used in the future⁴⁶.

Respondents' views

- 6.27. The majority of respondents who commented on this issue expressed their support for the introduction of the proposed condition. A summary of these views is presented in Chapter 4.

Ofgem's proposals

- 6.28. As set out in Chapter 4, Ofgem continues to consider it necessary to introduce new switch on/ switch off conditions that will apply to the standard special conditions in the licences of NTS and DN-GTs.
- 6.29. In order to achieve this, Ofgem is proposing to introduce three new standard special conditions to introduce a switch on / switch off mechanism for:
- ◆ standard conditions within Part A and B of the standard conditions within the GT licences (Part C is covered by the existing switch off/ switch on mechanism set out in Standard Condition 2 of the GT licence);
 - ◆ standard special conditions applicable to NTS and DN GT licensees (Part A of the proposed special conditions);
 - ◆ standard special conditions applicable to NTS licensees (Part B of the proposed special conditions);
 - ◆ standard special conditions applicable to DN licensees (Part D of the proposed special conditions).
- 6.30. Ofgem is therefore proposing to introduce three new standard special conditions:
- ◆ Application/Disapplication of standard conditions in Section A (Interpretation and Payments) and Section B (General) and

⁴⁶ In the September 2004 informal licence consultation document, Ofgem stated that it was satisfied that the introduction of this switch and the use of it in the context of DN sales would not cause any undue discrimination against IGTs (who would not have such a switch in their licences).

Application/Disapplication of standard special conditions applicable to both NTS and DN licensees;

- ◆ Application/Disapplication of standard conditions in Section A (Interpretation and Payments) and Section B (General) and Application/Disapplication of standard special conditions applicable to both NTS and DN licensees; and
- ◆ Application/Disapplication of standard conditions in Section A (Interpretation and Payments) and Section B (General) and Application/Disapplication of standard special conditions applicable to both NTS and DN licensees.

6.31. The drafting of these condition states that the Authority may, with the consent of the licensee:

- ◆ issue a direction to switch on and / or switch off (in whole or in part) standard special conditions and / or switch off (in whole or in part) standard conditions in sections A and B; and
- ◆ switch standard special conditions and standard conditions that have been switched off back on.

6.32. The drafting of these Standard Special Conditions A1, B1 and D1 is provided in Appendix 7B.

6.33. Ofgem invites respondents' views on its proposals for this new licence condition. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to DN sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Implementation of gateway requirements

September document

6.34. The September document stated that it may be necessary to develop new licence conditions that oblige NTS and DN-GTs to implement the gateway requirements⁴⁷ associated with the DN sales process. In this document, Ofgem stated that it is likely that such conditions would relate, without limitation, to the implementation of the Authority's decision regarding:

- ◆ the allocation of roles and responsibilities between the NTS and DNs;
- ◆ the agency and governance arrangements;
- ◆ the offtake arrangements; and
- ◆ the interruptions arrangements.

6.35. In addition, Ofgem indicated that it might be appropriate to introduce conditions to ensure that there is no undue discrimination between, for instance, IDNs and RDNs.

Respondents' views

6.36. Six respondents commented on this issue and some of them expressed some concerns on the implementation of gateway requirements, in particular in relation to the project's timetable.

6.37. One shipper/supplier stated that it was not convinced that all the issues identified as "gateway" requirement are necessary, and noted that only issues clearly identified as necessary should be included in the amended/new licences. In particular, the shipper/supplier expressed concerns in granting the Authority any broadly drawn powers to require development in given areas or introduce issues at a later date through this power. One potential purchaser expressed its concern that the implementation of some of these issues could delay completion and thus the realisation of the benefits from the process. The potential purchaser

⁴⁷ As outlined in the document *National Grid Transco – Potential sale of network distribution businesses, A Consultation Document*. Ofgem, July 2003.

underlined the necessity of a robust plan to deliver the arrangements and stated that all parties need to recognise the possibility of interim arrangements relating to gateway requirements.

- 6.38. Another potential purchaser stated that it would be extremely challenging to implement a full, working solution for the beginning of the next financial year, and noted that a pragmatic solution would be to introduce new licence conditions to reflect any necessary reforms that are unable to be completed until after the point when the Authority grants consent to Transco. On the other hand, one shipper/supplier considered that, in regard to the offtake and interruption arrangements, new licence conditions should be limited to the changes necessary to establish the new arrangements from day one, and it would be inappropriate to impose any licence conditions on licensees with regard to ongoing further reform.
- 6.39. As regards the content of the proposed new licence conditions, one shipper/supplier stated that it will be important to set out clearly the roles and responsibilities between the NTS and DNs. The shipper/supplier's main concern is to establish robust licence conditions to prevent DNs from taking energy balancing actions or being involved in speculative energy trading. The shipper/supplier also considered that a licence condition requiring transporters to use a common agent with respect to all central settlement activities is appropriate and, if each of these activities is properly defined under the UNC, a relevant reference could be included. The shipper/supplier noted that such a licence condition would avoid unilateral opting out of these common arrangements by transporters. One potential purchaser noted that it is essential that clarity on the potential new conditions that will cover the gateway requirements is obtained as soon as possible.
- 6.40. Another respondent considered that the implementation of interruption, offtake and flexibility arrangements could add significant costs to the industry with little associated benefit. The respondent expressed its preference for the de-linking of these issues and for a full consultation process including all potential signatories of any offtake code.

- 6.41. Finally, NGT stated that the gateway arrangements should be considered in relation to an appropriate implementation plan for the proposed new offtake and interruption arrangements.

Ofgem's proposals

- 6.42. Following consideration of respondents' views, and after further discussions at DISG, Ofgem proposes to introduce the following new licence conditions to reflect gateway requirements:

- ◆ a condition requiring DN-GTs to use reasonable endeavours to bring forward proposals for reform to interruption on the DNs with a view to potential implementation by 1 April 2006 consistent with DN obligations; and
- ◆ a condition stating that NTS and DN-GTs are not able to "opt out" of Agency Arrangements. This condition will also require agency services to be costed on an Activity Based Costing (ABC) basis, effective in the year 2005/6.

DN interruption reform

- 6.43. Ofgem notes the concerns expressed by respondents with respect to the introduction of conditions requiring future offtake or interruptions reform.
- 6.44. Ofgem considers that the reform of the arrangements for interruptions for sites connected to DNs is not necessary for the proposed transaction to proceed. For this reason, it has delinked the reform of the arrangements from the sales process.
- 6.45. Ofgem remains concerned that, in the longer term, inconsistency of approach between the NTS arrangements and DN arrangements for interruption could lead to inefficiencies and, ultimately, costs for customers. As such, Ofgem considers it appropriate to review the DN arrangements for interruption in the near future and therefore intends to place a licence condition on DNs to review the arrangements by April 2006. Any new reforms would need to address Ofgem's concerns in this area, and be consistent with GTs' statutory duties.

Furthermore, the review will be subject to the normal consultation process, including an impact assessment.

- 6.46. Ofgem is therefore proposing the introduction of a standard special licence condition applicable to all DN-GTs that places a reasonable endeavours obligation upon DNs to review and develop proposals for the reform of transportation arrangements relating to the interruption of supply points within the DNs with effect from 1 April 2006. Once such proposals have been brought forward, they will be subject to full consultation and impact assessment at that time.
- 6.47. The proposed drafting of this condition (Standard Special Condition D8 – Reform of Distribution Network interruption arrangements) is provided in Appendix 7B.
- 6.48. Ofgem invites respondents' views on its proposals for this new licence condition. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Agency obligations

- 6.49. Ofgem notes that during DISG meetings and in other consultation responses, shipper/suppliers have expressed concern regarding the possibility that DNs may be able to opt out of the proposed agency arrangements. Ofgem understands that were the proposed agency arrangements to fragment, this would have significant cost implications for shippers and ultimately customers. As such, Ofgem is proposing to introduce a new licence condition on the NTS and DN-GTs obliging them to operate through the Agency. It is Ofgem's proposal that the scope of the Agency will be defined within the Network Code proposed drafting of this condition (Standard Special Condition A14 – Agency Obligations) is provided in Appendix 7B. This drafting includes the following provisions:

- ◆ a provision requiring the economic and efficient operation of the agency;

- ◆ a provision requiring activity based costing of the agency; and
 - ◆ the transparent allocation of costs amongst relevant NTS and DN-GTs.
- 6.50. Ofgem invites respondents' views on its proposals for this new licence condition. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be consulted upon in February 2005. Further consultation may take place during this period through the DISG meetings.

Independence of the independent market for balancing

- 6.51. Following further consideration of the issues, Ofgem is proposing to create a new licence condition to ensure the continuation of a market for balancing that is independent from all NTS and DN-GTs.
- 6.52. The proposed drafting for this condition is provided in Standard Special Condition A16 – Independence of the Independent market for Balancing is provided in Appendix 7B.
- 6.53. Ofgem invites respondents' views on its proposals for this new licence condition. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.
- 6.54. The provisions relating to NTS and DN-GTs and the independent market for balancing are "augmented" for the NTS by NTS Special Condition C6 (Independent Market for Balancing). This is provided in Appendix 7B. The combined effect of these obligations is designed to replicate the current

provisions on Transco plc set out in Amended Standard Condition 9 of its GT licence.

Requirement not to prejudice the system of other GTs

September document

- 6.55. In the September document Ofgem indicated that a new condition might be needed to ensure that DN and NTS owners refrain from actions that could prejudice the safe and efficient operation of networks other than their own. Such a condition might also be needed as a reciprocal requirement for the NTS.
- 6.56. Ofgem invited views on whether a new licence condition obliging licensees not to act in a manner which could prejudice the safe and efficient operation of each other's systems could be introduced. This could be similar to the existing conditions in shippers' licences (e.g. Standard Condition 3 of the Gas Shipper's licences). If so, Ofgem considered that this should be a standard special condition on NTS and DN-GTs.
- 6.57. Ofgem considered that the potential proposal of a similar condition on IGTs with respect to the networks to which they are connected is not an issue that arises through the DN sales process. Further, Ofgem concluded that it would not be unduly discriminatory to propose such a condition on the NTS and the DN-GTs without proposing a similar condition for IGTs. Ofgem however invited views on this point.

Respondents' views

- 6.58. Two respondents considered that these conditions should also apply to IGTs. One shipper/supplier considered that this would help to address some of the inadequate contractual arrangements in the IGT CSEP⁴⁸ / NExAs. Another shipper/supplier suggested that the proposed conditions should address "broader" system issues as well as bilateral concerns between GTs. One shipper/supplier, while expressing its support for the proposed new licence conditions, asked for an explanation on how this licence condition may be enacted and for examples of scenarios where it may be invoked.

- 6.59. Two respondents suggested that the proposed licence conditions may not be necessary. One potential buyer suggested that this issue was addressed as part of the UNC licence obligation. The respondent stated that, irrespective of whether or not specific licence conditions are introduced in this respect, it will be necessary to ensure that all of the new framework and commercial agreements address liability issues associated within interconnecting networks. Another potential buyer considered that this condition will have a material impact upon others and its drafting will need to take this into account.
- 6.60. NGT expressed its support for a licence condition on this issue.
- 6.61. A draft version of the proposed licence condition, was circulated at DISG 24 and discussed at DISG 25. SSE expressed concern that the drafting of the condition was too general and MGN agreed that there could be some problems with the drafting of the conditions. It was noted that the licence drafting had been based upon the drafting included within the shipper's licence in relation to a similar obligation, and that shippers currently comply with the requirements of the licence. MGN questioned whether it is appropriate to adopt the provisions that apply to shippers given that the relationship between gas transporters is more interactive than the relationship between shippers and gas transporters.
- 6.62. The DISG also discussed whether it was appropriate for the requirement not to prejudice other networks to also apply to the provision, development and maintenance of other GT's pipe line systems. United Utilities and SSE both considered that these issues are dealt with elsewhere in the licence and hence should not be included.

Ofgem's proposals

- 6.63. Ofgem remains of the view that a new condition is required to ensure that NTS and DN-GTs do not prejudice the safe and efficient operation of each others' networks.
- 6.64. Following consideration of the views expressed at DISG by respondents to the September document, Ofgem has reconsidered the drafting of the proposed condition. The drafting of this condition draws on the wording included within

⁴⁸ Connected system exit point

Standard Condition 3 of the Gas Shippers licence. In Ofgem's view, use of such wording is appropriate, particularly given the fact that the DTI is currently consulting regarding the grant of an exemption to NTS and DN-GTs from the need to hold a shipper licence to allow them to make arrangements with each other for the offtake of gas from the NTS. Ofgem agrees with the views expressed through the DISG that the obligation should not relate to the planning, development and maintenance of other GT networks.

- 6.65. Ofgem has also considered whether this condition should also apply to IGTs. Ofgem continues to believe that it would be inappropriate to extend this proposed condition into IGTs' licences through the DN sales process in the interests of best regulatory practice.
- 6.66. A draft of this new condition in line with Ofgem's proposals is provided in Appendix 7B (Standard Special Condition A17 - General obligations in respect of gas transporters' pipe-line systems).
- 6.67. Ofgem invites respondents' views on its proposals for this new licence condition. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Inter-operator services agreements (including SOMSAs)

September document

- 6.68. If one or more DNs are sold, then it is likely that NTS and DN-GTs will enter into a variety of contracts for the provision of services. Chapter 4, sets out the background in relation to these proposals and the views of respondents' to the September document.

6.69. In Chapter 4, Ofgem sets out its view that it is not appropriate to regulate SOMSAs. These contracts are commercial agreements between the IDNs and the RDN business which the buyers have signed up to as part of the commercial arrangements associated with buying the DN and it is therefore not appropriate to be regulated. However, Ofgem states that we do not consider that these agreements will continue into the long term. If this is the case, we will review the need to regulate these contracts.

Ofgem's proposals

6.70. In light of Ofgem's proposals regarding SOMSAs set out in Chapter 4 of this document, the majority of the agreements will be unregulated and hence not require licence conditions. However, new licence conditions will be required in the following areas:

- ◆ to augment to provisions in Standard Special Condition 36 (Restriction on Activity and Financial Ringfencing) so that it accommodates income from new service agreements such as SOMSAs; and
- ◆ to introduce a licence condition requiring DNs to provide first line emergency response to the NTS.

6.71. As set out above, there is a need for the provisions in Standard Special Condition A36 – Restriction on Activity and Financial Ringfencing to be modified to accommodate income from new service agreements such as SOMSAs. As such, a new DN special condition has been drafted (Special Condition E1) to augment Standard Special Condition A36 for Transco's RDN business only, to allow an adjustment of the de minimis percentage restriction for a specified period such that in aggregate, de minimis turnover and investments do not exceed a specified amount for that period.

6.72. Ofgem notes that the specified dates and amounts have yet to be confirmed, but would welcome comments on the drafting provided for these conditions in Appendix 7B.

6.73. Ofgem invites respondents' views on its proposals for these new licence conditions. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG

meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Joint Office governance arrangements

September document

6.74. The Authority's Agency and Governance Arrangements decision document⁴⁹ sets out Ofgem's view that, in the event that the proposed sales proceed, a governance entity should be established in order to administer:

- ◆ the UNC modification process; and
- ◆ the process for introducing changes to network charging methodologies.

6.75. The governance entity is intended to increase transparency and visibility and reduce the potential for undue discrimination as proposed modifications would be administered in a consistent manner, regardless of the network operator concerned.

6.76. In the Final IA, Ofgem stated that the regulatory obligation to establish the governance entity would be introduced through a new licence condition applying to NTS and DN-GTs. It would be a matter for NTS and DN GT licensees to decide how to carry out these functions in a manner which is consistent with their licence obligations.

Respondents' views

6.77. Eight of the respondents, commenting on this issue, expressed their support for the proposed coordination role for the Joint Office.

6.78. The proposal for a Joint Office was originally consulted upon in the context of the Agency and Governance RIA. In responses to that document, over fifteen

⁴⁹ National Grid Transco Potential sale of gas distribution network businesses *Agency and Governance Arrangements Decision document* Ofgem Decision document 120/04

respondents expressed support for a model including a Joint Office, whereas only NGT and one shipper/supplier considered that the Joint Office was unnecessary.

- 6.79. After the Authority's high level decision in favour of a Joint Office, detailed proposals were developed through extensive discussions in the DISG. These discussions occurred between May and August 2004, where the group considered a number of options, ranging from a narrow Joint Office to a broad Joint Office. The key trade-off was the extent to which the Joint Office would be capable of exercising its functions independently, and the costs associated with procuring the necessary expertise. Some DISG participants, notably E.ON UK, supported a relatively broad approach in order to promote an independent governance regime. Conversely, NGT and SSE favoured a narrow approach because in practice, it would be very difficult (and costly) to find staff with the necessary expertise to carry out a governance function where issues only arise intermittently. A number of shippers also expressed the view that a broad Joint Office would be excessively costly. Ultimately a compromise was reached whereby all UNC participants could nominate Subject Matter Experts to support the Joint Office in the administration of the UNC modification process.
- 6.80. At DISG 22, NGT presented a draft version of the Joint Office Governance Arrangements licence condition. One shipper/supplier suggested that a provision should be added to ensure that documents associated with the joint governance arrangements are published, for instance on a Joint Office website.

Ofgem's proposals

- 6.81. In Appendix 7B, drafting for the proposed new licence condition: Standard Special Condition A12 - Joint Office Governance Arrangements is provided for comment.
- 6.82. This new licence condition, which is applicable to all NTS and DN-GTs, requires the licensee to establish, operate and develop arrangements for:
- ◆ the administration of the Network Code modification procedures;

- ◆ relating to the administration of the coordination of the modification of the licensee's and other GTs' relevant gas transporters' respective charges or reserve prices or charging methodologies;
- ◆ the administration of common systems arrangements;
- ◆ the administration of such matters as are provided for in the UNC; and
- ◆ the provision of efficiency in the implementation and administration of the Network Code.

6.83. The licensee is also required to enter into a Joint Governance Arrangements Agreement providing for the establishment and operation of the Joint Governance Arrangements. These Joint Governance Arrangements shall:

- ◆ ensure compliance with Network Code modification procedures;
- ◆ promote efficiency in the administration of the Network Code modification procedures so far as is consistent with the objective above; and
- ◆ avoid undue discrimination or preference as between the relevant gas transporters.

6.84. Ofgem believes that NGT's proposal to develop a 'Joint Office Governance Agreement', which all NTS and DN-GTs must be party to, is an appropriate vehicle for establishing the governance entity.⁵⁰ Among other things, the governance entity's governance arrangements should entrench its duty to act impartially in the exercise of its functions. The Joint Office should be funded by subscription fees in line with current NTS and DN price controls. NGT has not yet provided a copy of this agreement. It will be circulated for comment and consulted upon as soon as it is available.

6.85. A further feature of the proposed governance arrangements is that the joint office must exercise its functions independently and without undue regard to the interests of any particular party. Consequently, Ofgem believes that the Joint Office should be subject to structural separation from the GT licensees. This

includes information separation, separate staff and separate offices (or offices with separate security access).

- 6.86. Ofgem invites respondents' views on its proposals for this new licence condition. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Connections

September document

- 6.87. The background to this condition is set out in Chapter 4.

Respondents' views

- 6.88. Respondents' views on the consultation document are summarised in Chapter 4.

Ofgem's proposals

- 6.89. The new licence condition will impose overall standards of performance on all DN-GTs in relation to the following activities:

- ◆ the provision of quotations for providing new or altered connections;
- ◆ the provision of information in response to land enquiries and the approval or rejection of designs submitted by independent connection providers; and
- ◆ substantial completion of site works.

- 6.90. In each case the proposed overall performance target will be 90%.

⁵⁰ See NGT paper on the constitution and structure of the GT joint office, DISG 17.

- 6.91. Quotation performance will be measured in relation to the following customer groups:
- ◆ standard quotations for gas loads up to and including 275kWh per hour, i.e. a U24 meter;
 - ◆ non-standard quotations for gas loads up to and including 275 kWh per hour; and
 - ◆ non-standard quotations for gas load exceeding 275kWh per hour
- 6.92. The new standards will not apply to connections at pressures above 7 bar, to new multiple residential or industrial developments containing more than six premises or to complex connections, for example, connections involving railway crossings. DNs will be required to submit proposed categories of connection that should be classed as complex to the Authority for approval.
- 6.93. The new licence condition will also require the DN to provide:
- ◆ a scheme through which customers can challenge the accuracy of quotations and receive refunds in respect of incorrect quotations; and
 - ◆ specified information to the Authority on at least a quarterly basis and to carry out audits of samples of quotations as proposed by the licensee and agreed by the Authority.
- 6.94. The drafting of this condition (Standard Special Condition D10) is set out in Appendix 7B of this document.
- 6.95. Ofgem invites respondents' views on its proposals for this new licence condition. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Governance of technical standards

September document

- 6.96. In the September document, Ofgem suggested that it may be appropriate to develop a new licence condition relating to the governance arrangements applying to the technical specifications and operational procedures for making connections to networks. If there are multiple DN owners, different technical standards could be introduced. This could restrict the development of competition and efficient operation in these areas, as third party companies would be required to comply with differing standards depending on which network they are interfacing with.
- 6.97. To reduce the risk of this outcome, common governance arrangements could be adopted covering all specifications, procedures and accreditation schemes imposed by the DNs on third party companies who interface directly with their networks. This approach could involve the establishment of a review panel to manage the governance of standards and procedures, where the review panel includes representatives of network users and consumers as well as DNs⁵¹.
- 6.98. Ofgem invited views as to whether it is appropriate to introduce a new standard special condition applying to DN-GTs concerning the governance of technical standards. Ofgem also invited views on whether respondents consider this issue to be more appropriately dealt with elsewhere in the regulatory framework (for example by Health and Safety executive).

Respondents' views

- 6.99. Three respondents expressed their support for the introduction of a licence condition in relation to the governance of technical standards. British Gas Connections noted that in electricity different standards have served to obstruct competition and stated that the opportunity to move from a largely consistent approach to one where DNs can alter specifications, standards and procedures and thereby frustrate connection competition should be avoided. One

⁵¹ Ofgem introduced arrangements of this nature in the electricity industry in October 2002, however, the arrangements were documented through industry codes rather than through licence conditions. See *Governance of Electrical Standards, Final Proposals*, Ofgem, October 2002.

shipper/supplier supported a licence condition for DN-GTs concerning the governance of technical standards under the UNC with detailed arrangements set out in the UNC and not requiring the Authority's approval.

- 6.100. One shipper/supplier did not agree with the assertion that a company in single ownership automatically has one standard for an activity. The shipper/supplier noted that the development and coordination of technical standards need to be carried out in a careful and coordinated manner and stated that it would be appropriate to reference these issues in the licence but said that it is unclear whether the equivalent of the grid code for the gas industry is necessary. It should be noted however that a number of standards and codes of practice exist in the gas industry e.g. IGEM engineering standards and further work is under way with other independent bodies in support of safety cases obligations.
- 6.101. Four respondents considered that it was inappropriate to introduce a licence obligation regarding the governance of technical standards. One potential purchaser considered that such governance would be better effected through terms in relevant codes rather than in a licence condition. NGT suggested that these arrangements should be implemented through industry codes of practice (for example common operational procedures for live connection work and common competence validation process).
- 6.102. One potential purchaser noted that the introduction of such a condition would be onerous and could stifle development. The potential purchaser commented that the concerns over the possible restrictions to the development of competition arising from differing standards are not justified since all networks will be bound by the provisions in the Competition Act and part of the business separation provisions would introduce an obligation on each network owner not to restrict, prevent or distort competition. The potential purchaser stated that, to the extent that some form of coordination is required, it would be more appropriate to provide such provisions through industry codes, consistent with the electricity industry.
- 6.103. The Gas Industry Safety Group noted that any changes to standards applied to date will need to be justified so as to ensure that they will not lead to a less safe regime, and considered that this issue would be more appropriately dealt elsewhere in the regulatory framework.

Ofgem's proposals

- 6.104. Ofgem has given consideration to the views of respondents as set out above and recognises that there is a difference in opinion between those respondents who consider that a licence condition would be an important safeguard for competition in connections and those who consider that it could be onerous.
- 6.105. On balance Ofgem is persuaded that there are merits in introducing such a condition. Although we recognise that the GTs will be subject to the provisions of the Competition Act, Ofgem also considers that the move away from network wide technical standards could have a detrimental effect on competition if separate technical standards were to develop on separate networks.
- 6.106. Ofgem considers that the drafting of the condition must be such as to ensure that there is some uniformity in respect of the technical standards imposed by DNs without hindering innovation in connections and/ or interfering with the provisions of the DNs safety cases. Consultation on the drafting of the condition is therefore very important.
- 6.107. Ofgem is minded to introduce a new condition applicable to all NTS and DN-GTs regarding the technical specifications and operational procedures for making connections to networks. These provisions have yet to be drafted, but will be tabled for discussion at an upcoming meeting of the DISG.
- 6.108. Ofgem invites respondents' views on its proposals for this new licence condition. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Arrangements for gas measurement

September document

- 6.109. In the informal licence consultation document, Ofgem identified two key concerns regarding the arrangements for gas measurement:

- ◆ arrangements for testing measuring equipment at the NTS/DN interface; and
- ◆ arrangements for testing for water vapour.

6.110. Equipment installed at the NTS/DN interface measures the volume, energy content and characteristics of gas flows. These parameters have a direct impact on the volume of gas for which customers are charged, and consequently it is important that the measuring equipment is accurate. At present, the testing regime is based partially on a regime established by the Gas (Calculation of Thermal Energy) Regulations 1996. However, the powers granted to Ofgem under the Regulations are not comprehensive and consequently Transco has agreed with Ofgem to undertake regular independent audits.

6.111. Water vapour content has also a direct, though minor, impact on the quantity of gas for which consumers are charged, and historically, tests for the presence of water vapour in the distribution networks have been conducted. When water vapour is found in the distribution network, Ofgem issues Determinations under Section 12 of the Gas Act that reduce affected consumers' bills. Ofgem has historically monitored Transco's network at test points agreed with Transco.

6.112. Going forward, it is possible that the processes described above could break down if IDNs (or indeed Transco) were unwilling to participate in the informal arrangements. One option for addressing this risk would be to introduce new licence conditions to formalise the arrangements. However, in the case of arrangements for testing measuring equipment at the NTS/DN interface, Ofgem has expressed concerns that this approach could be overly prescriptive.

6.113. Ofgem invited views on whether it is appropriate to introduce a new licence condition that relates to the testing of measuring equipment. In particular, Ofgem invited views on whether respondents consider this issue could be more appropriately dealt with elsewhere in the regulatory framework, for instance in the UNC.

Respondents' views

6.114. Two respondents supported including the arrangements for gas measuring in the licence. One shipper/supplier stated that it would be logical to reference this

issue in the UNC, in the Offtake Code and in the licence. Another shipper/supplier added that a new licence condition would also be required to ensure that flows at all NTS offtakes (NTS direct connects and DN offtakes) are subject to accurate measurement. The respondent stated that this will be important in ensuring there is no undue discrimination between NTS connectees in relation to capacity or within-day flexibility services that may emerge.

6.115. Two respondents expressed their preference that this issue should be addressed within the UNC. One potential purchaser added that failure by a network owner to co-operate with respect to either of these issues could be construed as not complying with its duty to operate an efficient network, thus rendering the introduction of an additional licence obligation unnecessary.

6.116. NGT suggested that, given that the informal arrangements appear to be working at present, it would seem reasonable to continue with the present flexible process and only introduce a more formal approach should it prove necessary.

Ofgem's proposals

6.117. Following consideration of respondents' views, Ofgem is minded to require Transco plc to formalise current arrangements for testing measuring equipment within the UNC. As such, Ofgem is not proposing a new licence condition at this time.

6.118. With respect to the arrangements for testing for water vapour, Ofgem notes that an initial consultation document was published by Ofgem on this matter in September 2004⁵² following publication of the informal licence consultation. As stated in this document, it is Ofgem's current view that this scheme should be discontinued. As such, Ofgem does not believe that it is appropriate for this scheme to be formalised within a new licence condition at this time. However should the scheme be retained, Ofgem would consider issuing a further consultation with respect to creation of a new licence condition.

6.119. Ofgem invites respondents' views on its proposals in this area. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005.

If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

Separation of monopoly and competitive activities

September document

- 6.120. In the September document, Ofgem expressed the view that amendments to the business separation provisions could be required to deal with any potential competition issues which may arise when issues arising from the identity of potential purchasers had been fully considered. We suggested that this could involve the introduction of business separation requirements modelled on those that apply to electricity distribution network operators (DNOs).⁵³

Respondents' views

- 6.121. Respondents' views on this issue have been set out in Chapter 4 and 5 of this document.

Ofgem's proposals

- 6.122. Having considered respondents' views, Ofgem continues to consider that it is appropriate to update the business separation requirements to align the gas business separation requirements with those that apply in electricity. These conditions will replace Transco's existing conditions Amended Standard Condition 39 and Standard Condition 40.
- 6.123. The requirements that apply between electricity DNOs and their affiliated supply businesses are set out in an Ofgem decision document issued in February 2002.⁵⁴ The regime is designed to ensure that licensees:

⁵² Gas Quality, Wet Gas administration Scheme, Initial Proposals, 24 September 2004

⁵³ Ofgem, *Potential sale of gas distribution network businesses – Initial thoughts on restructuring of Transco plc's Gas Transporter Licences*, Consultation Document September 2004, pg 81.

⁵⁴ Ofgem, *Separation of PES business – Review of C39 of the proposed new distribution licence Decision Paper*, February 2002.

- ◆ put in place managerial and operational systems which prevent any relevant supplier or shipper from having access to confidential information except where:
 - ◆ the information is made available on an equal basis to any gas or electricity supplier or gas shipper; or
 - ◆ the information relates to a customer of the relevant shipper.
- ◆ manage and operate the distribution business in a way that does not restrict, prevent or distort competition in the supply of electricity or gas or the shipping of gas or the generation of electricity.

6.124. In addition, licensees are required to have in place a statement describing the practices, procedures and systems it has adopted to ensure that these conditions are met. The statement must be approved by the Authority and set out how the licensee shall maintain full managerial and operational independence of the distribution business from any relevant shipper or supplier, including separate branding, and (so far as is required to ensure compliance with these provisions) separate premises, systems, equipment, facilities and management and operations staff.

6.125. Licensees are required to take all reasonable measures to ensure that they comply with the statement, and must also publish the statement on their website.

6.126. Further, they must appoint (following consultation with the Authority) a compliance officer whose function is to facilitate compliance with the licensee's business separation and no undue discrimination obligations. The compliance officer must be given access to resources and information to enable him or her to fulfil his or her functions. Among other things, it is proposed that the duties of the compliance officer shall include:

- ◆ monitoring the effectiveness of the practices, procedures and systems adopted in accordance with the statement referred to above;
- ◆ investigating any complaints received in relation to the licensee's business separation arrangements; and

- ◆ providing an annual report to the directors of the licensee.

- 6.127. Finally, the licensee must provide an annual report to the Authority setting out its compliance with the business separation and no undue discrimination obligations, and its compliance with the statement.
- 6.128. Ofgem notes that Amended Standard Condition 39 contains certain additional provisions relating to storage and metering which have no equivalent within the electricity DNO regime. In making the proposed changes, it is important to accommodate these arrangements.
- 6.129. Ofgem does not propose to introduce new conditions relating to the separation of NTS and DN GTs from affiliated IGTs. Rather, Ofgem considers that the non-discrimination provisions within the existing regime together with Ofgem's wider competition powers are sufficient to address such concerns. However, Ofgem welcomes respondents' views on this issue.
- 6.130. The proposed drafting for these conditions (Standard Special Conditions A33 (Restriction on Use of Certain Information and Independence of the Transportation Business) and A34 (Appointment of Compliance Officer)) is provided for comment in Appendix 7B.
- 6.131. As discussed in Chapter 4 to address the issue of LNG a new NTS special condition has been introduced to augment this standard special condition with LNG provisions (Special Condition C1, paragraph 11).
- 6.132. Ofgem invites respondents' views on its proposals for this new licence condition. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties thorough its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be consulted upon in February 2005. Further consultation may take place during this period through the DISG meetings.

Separation of NTS and RDNs

September document

6.133. The September document reflected the Authority's "minded to" position to require Transco to undertake legal separation and targeted structural separation.

Respondents' views

6.134. Respondents' views on this issue are set out in Chapters 4 and 5.

Ofgem's proposals

6.135. This section describes Ofgem's proposals for separation between Transco's NTS and RDN businesses.

6.136. As explained in Chapter 4, to separate structurally Transco's NTS and DN businesses, Ofgem proposes to introduce new conditions that are the business separation regime that currently applies between electricity DNOs and affiliated supply businesses, recognising that the scope and scale for the potential undue discrimination could differ between monopoly and competitive activities rather than between one network monopoly and another.

6.137. These licence conditions would be introduced as a special condition in Transco's NTS licence. In addition, a special condition would be imposed in Transco's DN licence requiring the RDNs to use all reasonable endeavours to comply with the statement produced by the NTS pursuant to its licence obligations.

6.138. Ofgem intends to present an initial draft of this proposed licence condition to the DISG and to invite comments.

6.139. Ofgem also proposes to insert a special condition in Transco's NTS licence that requires Transco:

- ◆ to establish a set of arrangements between the NTS and the RDNs which are not unduly different from the contractual arrangements entered into with IDNs. Ofgem intends to produce drafting on this condition and consult through DISG.
- ◆ to obtain an undertaking from its parent company to apply the arrangements between the NTS and RDNs on the same basis as contracts entered into with non-affiliated businesses. A draft of this condition is

provided in Appendix 7B NTS Special Condition C19 (undertaking for Ultimate Controller concerning non-discrimination between the NTS transportation activity and the distribution network transportation activity).

- 6.140. Another potential amendment which seeks to largely emulate the benefits of legal separation relates to regulatory accounts. Ofgem is proposing to require Transco to submit separate regulatory accounts for its NTS and (each individual) RDN business that are in the same format as statutory accounts. As part of its Distribution Price Control Review, Ofgem is consulting on a licence amendment that requires electricity DNOs to submit regulatory accounts in the same format as statutory accounts.⁵⁵
- 6.141. Ofgem also intends to introduce a licence condition that seeks to largely recreate the benefits of legal separation in terms of robust corporate governance. This could include, among other things, conditions which seek to relate director's duties to each DN. This approach was suggested by a potential purchaser at DISG 7 and has been adopted in the water industry.⁵⁶ Ofgem could also seek to promote good corporate governance using provisions to improve the use of Transco's compliance officer. Ofgem intends to present an initial draft of any proposed licence conditions on corporate governance to the DISG and to invite comments.
- 6.142. Ofgem invites respondents' views on its proposals for these new licence conditions. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult with interested parties thorough its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be consulted upon in February 2005. Further consultation may take place during this period through the DISG meetings.

⁵⁵ The proposed changes, which relate to Standard Condition 42 of the DNO licence, are due to be published in the week commencing 29 November 2004.

⁵⁶ *Potential sale of gas distribution network businesses – Final Impact Assessment – Appendices* November 2004, pg 120.

LNG Storage

September document

6.143. Within its informal licence consultation Ofgem detailed that NGT was of the opinion that the most appropriate location for the licence obligations relating to LNG Storage should be Transco plc's NTS-GT licence only in view of the fact that such facilities are connected to the NTS.

Respondents' views

6.144. The views of respondents relating to the treatment of LNG Storage are set out in Chapter 4.

Ofgem's proposals

6.145. As set out in Chapter 4, Ofgem considers it to be appropriate for obligations relating to LNG Storage to sit within the NTS licence only. As such, Ofgem is proposing a new special condition upon the NTS, which seeks to "augment" the following standard special conditions:

- ◆ Standard Special Condition A3 - Definitions and Interpretation;
- ◆ Standard Special Condition A4 - Charging Gas Shippers – General;
- ◆ Standard Special Condition A5 - Obligations as Regard charging Methodology;
- ◆ Standard Special Condition A6 - Conduct of Transportation Business;
- ◆ Standard Special Condition A7 - Requirement to Enter into Transportation Arrangements in Conformity with the Network Code;
- ◆ Standard Special Condition A11 - Network Code;
- ◆ Standard Special Condition A26 - Provision of Information to the Authority;
- ◆ Standard Special Condition A27 - Disposal of Assets;

- ◆ Standard Special Condition A30 - Regulatory Accounts;
- ◆ Standard Special Condition A32 - Definition of Permitted Purpose;
- ◆ Standard Special Condition A33 - Restriction on Use of Certain Information and Independence of the Transportation Business;
- ◆ Standard Special Condition A37 - Availability of Resources;
- ◆ Standard Special Condition A41 - Emergency Services to or on Behalf of Another Gas Transporter;

6.146. Drafting for this new “augmenting” provision (Special Condition C1 – Amendments to standard conditions and standard special conditions applicable to the licensee) is provided in Appendix 7B.

6.147. Ofgem invites respondents’ views on its proposals for this new licence condition. Following consideration of respondents’ views, where necessary and appropriate, Ofgem will consult with interested parties through its DISG meetings in January 2005. If the Authority grants its consent to any DN Sales then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated Section 23 notice) will be published in February 2005. Further consultation may take place during this period through the DISG meetings.

7. Way forward

7.1. As described previously, this document consults upon two sets of changes:

- ◆ it consults formally upon changes to Special Conditions 28A, 28B, 29, 30, 33, 34, 35, 36, and Schedule A of Transco plc's six GT licences in accordance with Section 23 of the Gas Act; and
- ◆ it consults informally on a range of further changes to Transco plc's six GT licences that would be required to create a licensing structure that can support DN sales so that customers interests are protected.

7.2. As set out in Chapter 1, Ofgem welcomes views on this document, to be received:

- ◆ by close of business on 23 December 2004 in the case of the formal Section 23 consultation (which is discussed in Chapters 1 to 3 and Appendix 4); and
- ◆ by close of business on 7 January 2005 in the case of the informal Section 8AA consultation (which is discussed in Chapters 4 to 6, and Appendices 5 and 6).

7.3. Where necessary, those conditions that are flagged as requiring further development, are intended to be discussed thoroughly at DISG in the forthcoming weeks and into the new year.

7.4. Following consideration of respondents' views, where necessary and appropriate, Ofgem will consult further with interested parties through its DISG meetings in January 2005. In order to facilitate this, Ofgem will publish a timetable for consideration of these licence conditions at DISG meetings at the beginning of January 2005.

7.5. If the Authority grants its consent to Transco in relation to the disposal of DN assets then it is expected that the formal consultation in relation to these proposals (pursuant to a Section 8AA notice and an associated additional Section 23 notice) is expected to be published in February 2005. Further consultation may take place during this period through the DISG meetings.

7.6. Table 7.1 sets out the way forward in relation to the formal steps involved in the restructuring of Transco plc's six GT licences in connection with DN sales.⁵⁷

Table 7.1 Restructuring of Transco plc's six GT licences - summary of way forward

STEP 1 Amendment of licences in accordance with Section 23 notice	In the event that the Authority consents to the proposed disposal of DN assets then, subject to consideration of responses, the Authority would issue directions to bring into effect the modifications to Transco's six GT licences in accordance with the Section 23 notice published with this document. If respondents raise any significant issues, a further Section 23 notice may need to be issued.
STEP 2 Issue consultation on transfer of licences to wholly owned Transco entities	Transco applies for four of the new DN-GT licences to be transferred to four wholly owned Transco subsidiary companies and there is a two month formal consultation under Section 8AA of the Gas Act relating to the transfer of four of the DN-GT licences from Transco to the four Transco subsidiary companies (and an accompanying additional Section 23 notice in respect of changes to the NTS and RDN licences that are being retained by Transco).
STEP 3 Transfer of licences	Subject to responses received in the Section 8AA consultation process, the four amended DN-GT licences are transferred to Transco's wholly owned DN subsidiary companies.
STEP 4 Consent to sale of shares in DN companies to purchasers	It may be necessary to introduce further changes to six GT licences (both those that may have been transferred to wholly owned Transco subsidiaries and those that have been retained by Transco) as part of the Authority's consent to Transco to dispose of the shares in the subsidiary companies to third party purchasers.

7.7. The various steps associated with the licence amendment process are described in more detail in two open letters published on Ofgem's website.⁵⁸ Transco's work plan for the various aspects of the DN sales process is set out in Appendix 1.

⁵⁷ It should be noted that each of the steps set out in Table 7.1 will only go ahead if the Authority decides to consent to DN sales. The Authority is expected to consider whether or not to consent to DN sales in mid January 2005.

⁵⁸ Ofgem open letters *Licence Amendment Process* (5 August 2004), *Updated timetable for Potential Gas Distribution Network Sales Project* (15 October 2004). These documents are available on the gas distribution network sales page of Ofgem's website.