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to customers*

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Dear Chris,

Open Letter to Transco in relation to the UNC Review of Governance Arrangements

I refer to the letter from Alan Raper dated 25 January 2005, which set out the position of a number of UNC Development Forum attendees (listed in the letter) in relation to the UNC governance arrangements and, in particular, the role of the Panel. The letter provided us with useful feedback from market participants in advance of the consultation that we plan to issue on UNC matters in March 2005. Given that the letter was sent on behalf of a number of industry representatives, our reply will be posted as an open letter on Ofgem's DN Sales website.

Before commenting on the issues raised in that letter, it is important to note that nothing in this letter fetters the discretion of the Authority in relation to:

- ◆ any future decisions to be taken in relation this issue of governance; and/or
- ◆ to DN sales more generally,

including without limitation, any decisions in respect of the proposed licence modifications and/or any modifications which may be proposed to the Network Code, the proposed Uniform Network Code (UNC) and/or the various short form codes.

Scope of changes to the modification rules

As you will be aware, the governance arrangements set out in the Ofgem position paper¹, which were discussed at the UNC Development Forum on 18 January, are the output of several months of work by the DISG. These proposals have not been developed for the purpose of responding to potential changes to the appeals mechanism, but rather to address the issues associated with the creation of a divested industry structure incorporating multiple Gas Transporters, and concerns that a number of shipper participants have raised as part of this process.

¹ *Ofgem preliminary position on the Uniform Network Code modification process & the constitution of the governance entity*, DISG 15, August 2004.

Whilst Ofgem notes that in developing their position, UNC Development Forum attendees have had regard to the Department of Trade and Industry's consultation regarding the Code Modification Appeals Procedure, we consider that any amendments to the governance arrangements associated with the introduction of such an appeal mechanism should be considered outside of the DN Sales process.

Therefore, Ofgem remains of the view that changes to the governance regime, as described in the position paper, are a critical element of the reforms required to ensure that customers' interests are protected in a multi-transporter industry framework. In particular, the changes to the governance regime seek to ensure that governance processes are transparent and administered in a consistent manner. Ofgem considers that this should reduce the potential for discrimination and partiality in these processes and should therefore protect the interests of customers within a divested industry structure.

The role of the panel

As noted in the Ofgem position paper, the Panel has a variety of functions which have important interactions with other aspects of the operational and regulatory arrangements. In addition to functions relating to the publication of modification reports and making recommendations to the Authority in relation to modification proposals, the Panel will be responsible for:

- ◆ determining a schedule for each modification proposal within minimum and maximum limits for assessment of non urgent modification proposals set out in the modification rules;
- ◆ establishing the terms of reference and the associated timetables when referring proposals for development through workstreams; and
- ◆ approving a list of independent experts to be engaged by the governance entity as and when required (subject to a maximum annual budget approved by the governance entity's board of directors).

Consequently, the Panel will have a major role in determining the activities of the Joint Office. In the absence of more balanced representation on the Panel, independent distribution network owners (IDNs) will have limited opportunities to help determine the activities of the Joint Office, even though they bear a proportion of its cost.

Further, under proposed Standard Special Condition A15, the scope of the services and systems to be provided by the Agency are set out in the UNC. Again, this means that decisions made via the modifications process have the potential to impact on IDNs' costs and as such IDNs should be able to contribute towards the modifications process in a manner that is commensurate with the opportunities afforded to other parties.

Interested parties have had several opportunities to contribute to the UNC governance debate. Governance was regularly discussed at the DISG between May and September 2004 and the outcome of those discussions was consulted upon in the Final Impact Assessment.² Ofgem does not consider that it is appropriate to reopen the governance debate at this stage, and further, it should be noted that to do so would require further consultation. Ofgem recognises, however, that a number of detailed issues associated with the UNC governance arrangements are not

² Ofgem *National Grid Transco - Potential sale of gas distribution network businesses Final Impact Assessment* November 2004, pgs 83-84.

addressed in the position paper. These issues should be addressed through the standard UNC modification process.

If you have any questions on this matter, don't hesitate to contact me or Jessica Hunt on 0207 901 7431.

Yours sincerely

Sonia Brown
Director, DN Sales