



Sonia Brown
Director, Transportation
Ofgem
9 Millbank
London SW1P 3GE

11 April 2005

Dear Sonia

Uniform Network Code Second Consultation

I write in response to the second consultation by Ofgem relating to the proposed drafting of the Uniform Network Code (UNC) to be put in place in preparation for NGT's proposed sale of four of its distribution networks (DNs). Shell Gas Direct (SGD) objects to the implementation of the UNC in its current form. We comment on this further below but note that our comments should not be read as acknowledging the processes leading to, nor acceptance of, the policy decisions behind the legal drafting. SGD reserves the right to challenge the Authority's decisions on UNC and associated modification 0745.

Process for consultation

We have read the responses from both Ofgem and NGT in respect of the first consultation which we found unconvincing in certain aspects. We have no further comments to make on the UNC drafting itself and consider that the majority of that document provides a satisfactory contractual framework for the industry in the post-DN Sale environment.

However, we are not convinced by either Ofgem nor NGT's response to some of our specific concerns about the process adopted. We remain of the view that instead of the expected four week consultation, we are being asked to take part in 2 two week consultations. Ofgem and NGT may consider this a "five week process" but this does not reflect what is being asked of shippers and other interested parties to provide comments in two weeks if we wanted to "afford an opportunity for Transco to update the documents mid-way through the consultation process" or "to help shape the document". We interpret this as meaning that if we wanted to have a good likelihood of our comments being included in the final legal drafting, we needed to respond within 2 weeks.

We remain of the view that Ofgem has only provided two 2 week consultations. While Ofgem may have a different view, we cannot see how Ofgem can disagree with others' perceptions – what can be concluded is what Ofgem meant to communicate and what was understood by many differs. We remain of the view that a much earlier indication of this "enhanced" process would have improved our ability to prepare for, and respond to, the consultations. We would welcome the Authority's views on how it considers Ofgem to have met the requirements of best regulatory practice. The existence of open meetings are, in themselves, insufficient to address this concern.

We continue to be of the view that a formal consultation on any changes to the governance of the Code needs to be carried out. This process is not a consultation on policy but on legal drafting: there has been no consultation on approach to governance of the UNC. We note that when Ofgem presented its paper to the DISG meeting, they stated that "Ofgem intends these views will be incorporated into detailed proposals that will be subject to public consultation." We comment further on whether Ofgem should be directing that its views on preferred governance were required but question not here that there has yet to be the intended public consultation. If the views of the UNC group had been taken on board, this consultation on drafting would be in relation to the governance that is currently in place for the Network Code.

Exit & offtake arrangements

We re-affirm our view that the proposals by Ofgem and being implemented by NGT are not necessary to allow DN Sales and, indeed, the rush to implement in September has had a negative impact on shippers and other interested parties ability in being able to to prepare for and contribute to the DN Sale process. We will be raising further concerns regarding the proposed changes in our response to Ofgem's consultation on proposed transporter licence conditions associated with the new industry structure.

In particular, we note that while consultation on the UNC has undertaken, NGT has also arranged a number of meetings to discuss the exit changes, pricing changes etc. This has stretched resources and cannot be considered an adequate substitute for a genuinely open process. We remain perplexed as to why the Authority considers a rushed process to be necessary or efficient.

Governance

The proposals made by Ofgem and NGT jointly for the governance of the UNC continues to raise concerns regarding due process. We reiterate that our comments should not be read as acceptance of the approach used by Ofgem and by Transco to introduce these drafting changes.

Chris Train states in his letter of 29 March 2005 that NGT is "firmly of the view that the current arrangements need to be reformed to support the new industry structure". NGT's view alone can not sufficient to result in only its proposals being put forward. NGT has repeated the views expressed by Ofgem on why the structure adopted is the preferred one. This does not address the failure to consult the industry by starting with which changes in the structure require changes and what the best way forward is. Instead, NGT appears to have taken Ofgem's suggestions as a requirement and avoided necessary consultation on changes to this contract. We know of no commercial parallel where one organisation can impose such a change to governance on other parties to a contract. The proposals may be acceptable to DN purchasers but that their views are not relevant for the interests of shippers, nor the right of all parties to the Code to be consulted.

As Ofgem and NGT will know, the Gas Forum conducted a review of the governance of the Network Code in 2004. This was carried out through seminars open to all shippers (not just members of the Forum). Through this process, a number of options were discussed including whether there should be a panel recommendation and whether the panel itself should be reconstituted to have sectoral representation. The attendees did not consider that these options were worthy of further action and therefore did not put forward such proposals. Forum members have put forward a number of proposals to improve the governance of the Code. All of these proposals have gone through the established governance process leading to some being accepted by Ofgem and others rejected. We do not see that the sale itself requires the established procedures to be circumvented.

NGT states that since “*a mechanism to establish a single Transporter recommendation would be required, we believe it is both economic and efficient for the Transco recommendation to be replaced by a Panel recommendation*”. We cannot identify the reasoning behind NGT arriving at its belief. It would be more economic and efficient for the Transporters to come up with a process themselves rather than forcing the shippers to take part in a complex, inefficient new arrangement. It cannot be too difficult for NGT and the new iDNs to think up a process between themselves. The approach NGT is advocating will result in final modification reports being delayed by a month as they go through the new, convoluted process (one reason why this was rejected by shippers who participated in the Gas Forum discussions). We cannot see that this can be described as improving efficiency nor that it can be “economic”.

The only impact the recommendation has is to produce legal drafting and as the Transporters will normally be paying for the production of such drafting (through the Joint Office), we see no reason for shippers to get involved at all. While NGT claims that it is not prejudging the DTI approach, it is difficult to understand why it is so insistent on having a panel recommendation without this change. As both NGT and Ofgem consider the process so far to be open, we would welcome transparency on the number of discussions Ofgem and NGT have had with the DTI both individually and/or jointly regarding the expected Statutory Instrument to introduce appeals to Code modification decisions.

Furthermore, as NGT recognises that the DTI will be coming forward with its proposals to allow parties to appeal Ofgem’s decisions on code modification proposals. Given that there may need to be changes to the governance to accommodate this, why insist on implementing Ofgem and Transco’s preferred solution now? The contractual commitment that NGT has made in the transitional document to bring forward a review once the appeals process is known is essentially *valueless*: it adds nothing. Such a review could be taking place now through the Governance workstream; or preferably it could have already taken place. We understand that this topic has already been raised and any shipper (or GT) could raise a proposal to consider the issue in any case. NGT’s commitment only delays and displaces proper consultation on the entirety of the changes. We note that both Ofgem and NGT publicly did not support the DTI’s implementation of Code appeals.

We are concerned that any discussions about having an independent chair (which the Forum group also considered but rejected) could delay implementation of the appeals process. We consider the right to appeal (in certain circumstances) essential for ensuring that Ofgem makes the best decisions. NGT does not indicate by whom such an “independent” voting member of chair would be appointed. We assume that NGT would consider an appointment process led by the Gas Forum and made by shippers a satisfactory outcome.

NGT makes reference to the fact that EON submitted a paper on governance to DISG. We do not purport to speak on behalf of EON but we understand from them that they had not intended their paper to be representative of industry views and that their paper was based on the assumption that the DTI appeals issue would be understood before their proposal was implemented. As this is not the case, their paper is not relevant to NGT’s argument in favour of pushing forward with its preferred solution.

We note again that Ofgem’s comments regarding whether it has fettered the discretion of the Authority. We assume that the Authority will be made fully aware that shippers have been asked to comment only on one option for the governance, that this option follows that set out by Ofgem as satisfying its criteria established by Ofgem and that proposals made by a number of shippers to adopt a different approach were rejected by Ofgem. SGD had raised concerns as an Ofgem staff member had suggested in February that the Authority would be “surprised” to learn that consultation had not already taken place although there is no reference to this in the Authority’s decision document on the sale. The Authority will understand that for a review

of the governance in relation to the appeals mechanism to take place no contractual commitment from NGT is necessary.

The Authority has reiterated in its final corporate strategy that “*Ofgem's role in the code modification process is limited to the Authority directing any final independent decision. Ofgem does not consider that it would be appropriate for the Authority to move away from this role at present, despite continued developments in energy markets. Ofgem considers it has an important role to ensure that code modifications are pro-competitive, maintain security of supply and are consistent with not only the codes' relevant objectives but also the statutory duties of the Authority which are designed to protect the interests of consumers.*” Ofgem appears to have gone somewhat beyond the limited role suggested in this paragraph by setting out what it considers to be the governance that meets the objectives and providing wider criteria to be met. We consider that only the parties to the contract (shippers and gas transporters) should come up with criteria and proposals. It is then for the Authority to make a decision without Ofgem directing what proposals should be put forward. While Ofgem may consider its approach to be the one that best addresses the objectives and the Authority's duties, this implies a more interventionist approach than what the Authority describes.

Conclusion

Shell Gas Direct reiterates that it has no objection to the sale of four of the gas distribution networks by National Grid Transco. However, we remain firmly of the view that only changes necessary for the sale itself should be implemented through this process. We strongly recommend that the governance under the Network Code is adopted until an open, transparent process is used to amend the governance arrangements. We repeat again that the transitional arrangements related to offtake pre-supposes implementation of modification proposals not yet raised. We will return to this issue in our response to the gas transporter licence conditions later this week.

Yours sincerely

*This letter is sent electronically
and therefore is not signed.*

Tanya Morrison
Regulatory Affairs Manager