

MGN Gas Networks (UK) Limited

Level 30
CityPoint
1 Ropemaker Street
London EC2Y 9HD
UNITED KINGDOM

Telephone 44 20 7065 2000
Facsimile 44 20 7065 2041
Internet <http://www.macquarie.com/uk>

17 March 2005

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

Dear Sonia

POTENTIAL SALE OF GAS NETWORK DISTRIBUTION BUSINESSES

**OFGEM CONSULTATION: FORMAL CONSULTATION UNDER SECTION 23 AND
SECTION 8AA OF THE GAS ACT 1986**

This document is the formal response to the above consultation by MGN Gas Networks (UK) Limited (MGN). MGN has signed an Option Deed with National Grid Transco (NGT) to acquire the Wales and the West (W&W) Distribution Network (DN) being sold by NGT. The transaction is conditional on a number of events, including the consent of the Gas and Electricity Markets Authority.

Please feel free to contact either Ed Beckley (020 7065 2039) or Julian Bagwell (020 7065 2412) should you wish to discuss any of the contents of MGN's response to your consultation.

Yours sincerely
MGN Gas Networks (UK) Limited

Howard Higgins
Division Director

Edward Beckley
Senior Manager

POTENTIAL SALE OF GAS NETWORK DISTRIBUTION BUSINESSES

OFGEM CONSULTATION: FORMAL CONSULTATION UNDER SECTION 23 AND SECTION 8AA OF THE GAS ACT 1986

MGN GAS NETWORKS (UK) LTD RESPONSE TO CONSULTATION

Ofgem has published a substantial set of documents relating to the draft licences that will apply to the gas distribution network owners in the near future. Our comments on these documents are set out below.

SSCA38 Credit Rating of the Licensee

As we have previously pointed out, the revised drafting has the effect of excluding all rating categories other than an issuer credit rating. Amongst other things, we believe for example that this excludes all Standard & Poor ratings, as it does not provide an issuer rating; if so, then this makes the separate reference to that agency in paragraph 2(a) otiose. The category that we intend to seek from Moody's, a Senior Implied Rating, is one that you have advised us is acceptable; if so, we do not see why it should be excluded on the face of the licence condition. Whilst you have said that you intend to issue us with an exemption or derogation letter in relation to this rating, we think it better to make explicit in the licence what ratings are and are not accepted. We also believe it helpful for the condition to leave some flexibility for any future rating category that is issued and that may satisfy your requirements.

We understand that the reason for the proposed drafting is to align the gas and electricity distribution licences. In general we have accepted the need for alignment, and have made comments on a number of other Conditions where amendments have been proposed to achieve this. We do not think it appropriate to align the licences in this area, however, because of the effects of what we have been told is an unintended consequence. More generally, we think it inappropriate regulatory practice to propose a revised condition, with an effect not intended, and then to offer exemption from it – if the Condition is inappropriately worded, we believe it would be better to amend it now, whether or not that causes alignment difficulties.

Because the category that we intend to seek is excluded by virtue of the new licence drafting we think that the effects of this drafting are material. We do not believe this to be a minor change, as stated in the Consultation Paper, paragraph 4.732.

Finally, the change necessary to get the draft Condition back to the point where it includes, rather than excludes, a number of ratings categories including a Senior Implied rating, is to delete the word 'issuer' from the phrase 'issuer credit rating'. We appreciate, however, that Ofgem is sensitive to providing allowance for ratings that do not reflect the underlying credit capacity of an issuer. An alternative would be to avoid the 'sunset' provision in proposed Special Condition E11 in our licence, in other words using the power in paragraph 2 of that condition to permit it to continue in being after the transfer of ownership. This would specifically provide for Ofgem to be able to accept Moody's senior implied rating and any other rating category that other agencies issue in the future with the intent of mirroring a senior implied rating, although it would not be specific about such ratings on the face of the licence.

SSCD4 Prohibited Procurement Activities

We understand the intent of D4 and agree with it. We are not sure whether or not as worded it precludes any capacity trading that we might in future undertake as part of the enduring offtake arrangements, especially to conform with any incentives scheme that may apply to us. Whilst this condition allows the Authority to provide written consent for such trading, if it is an integral part of the operation of the network we would prefer that it is clear on the face of the licence that it is permitted.

Other Comments

The draft licence conditions have already been the subject of extensive consultation, including two earlier rounds of full or close to full drafts, and a number of discussions on individual conditions at various Development and Implementation Steering Group meetings. MGN has contributed fully to that debate, and a number of the points that we have made have been reflected in revised drafting. At this stage, we do not think it appropriate to comment on each draft condition, given the degree of consultation to date, nor do we wish to repeat comments that were not previously accepted by the Authority.

We will respond to the recent Open Letter on the Long Term Development Statement within the timescales required – at this stage we envisage that our response will be to support the proposals generally, but to suggest that scope is limited to an appropriate level of granularity.

END