

Notice under section 23(1)(b) of the Gas Act 1986
Proposal to modify licences granted or treated as granted under
section 7 of the Gas Act 1986

The Gas and Electricity Markets Authority (the "Authority") hereby gives notice pursuant to section 23(1)(b) of the Gas Act 1986 (the "Act") as follows:

1. The Authority proposes to modify the licences (the "Licences") granted or treated as granted by the Authority under section 7 of the Act to all gas transporters.
2. The proposals are to modify the following standard conditions (the "Conditions") in Section C of the Licences -
 - (a) Condition 43 (Restriction on Activity and Financial Ring Fencing);
 - (b) Condition 44 (Availability of Resources);
 - (c) Condition 46 (Credit Rating of Licensee); and
 - (d) Condition 47 (Indebtedness),

as set out in Schedule 1 to this notice.

3. In summary –

- (a) the Authority proposes, in order to protect the interests of consumers, to introduce modified financial ring fencing arrangements for new and existing independent gas transporters, being those licensed gas transporters for whom in September 2001, the Secretary of State did not provide for Section C to have effect in their Licences by a scheme made under Schedule 7 of the Utilities Act 2000, but which in relation to each existing gas transporter, the Authority issued a Transportation Services Direction bringing Section C into effect on 19 January 2006 ;
- (b) The proposed modifications will align the financial ring fencing conditions in independent gas transporter Licences with the financial ring fencing conditions in all other gas transporter Licences granted or treated as granted under section 7 of the Act and in all transmission and distribution licences granted or treated as granted under sub-paragraphs (b) and (c) respectively of section 6(1) of the Electricity Act 1989; and

the reasons for these modifications are fully set out in documents published by the Authority, including -

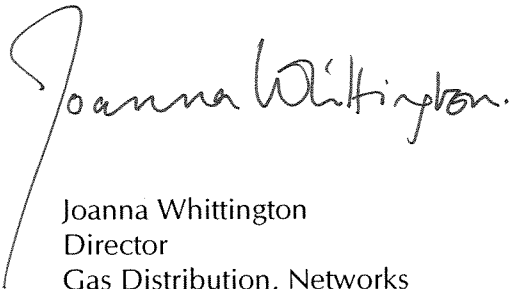
- (i) *The regulation of independent gas transporter charging – Draft proposals, December 2002 87/02;*
- (ii) *The regulation of Independent gas transporter charging – Final Proposals – July 2003, 64/03;*
- (iii) *Financial ring fencing for new and existing independent gas transporters – Initial proposals – November 2004, 205/04; and*

*(iv) Financial ring fencing for new and existing independent gas transporters –
Final proposals – September 2005, 209/05,*

copies of which are available (free of charge) from the Ofgem library, 9 Millbank, London SW1P 3GE (020 7901 7003) or the Ofgem website (www.ofgem.gov.uk).

4. The effect of the proposed modifications is to implement changes to independent gas transporters' financial ring fencing conditions, which were developed in order to protect consumers connected to their networks by providing safeguards for the financial stability of each gas transporter against any financial pressures arising from its affiliates.
5. "Relevant licence holders" for the purpose of giving notice of objection to the modification proposals are all and any gas transporters in whose Licences the conditions are in effect (pursuant to the Transportation Services Directions issued by the Authority on 18 January 2006) on the expiration of this notice.
6. A pro forma that a relevant licence holder may wish to use in order to give notice of objection is given in Schedule 2 to this notice.
7. Any representations or objections to the proposed licence modifications must be made in writing on or before 23 February 2006 and should be addressed to Samanta Padalino, 9 Millbank, London SW1P 3GE (020 7901 7033) or samanta.padalino@ofgem.gov.uk.

Dated 23 January 2006



Joanna Whittington
Director
Gas Distribution, Networks

Authorised on behalf of the Authority

Schedule 1

[Licence modifications]

Condition 43. Restriction on Activity and Financial Ring Fencing

1. Save as provided by paragraphs 3 and 4, the licensee shall not conduct any business or carry on any activity other than the transportation business.
2. The licensee shall not without the prior written consent of the Authority hold or acquire shares or other investments of any kind except:
 - (a) shares or other investments in a body corporate the sole activity of which is to carry on business for a permitted purpose;
 - (b) shares or other investments in a body corporate which is a subsidiary of the licensee and incorporated by it solely for the purpose of raising finance for the transportation business; or
 - (c) investments acquired in the usual and ordinary course of the licensee's treasury management operations, subject to the licensee maintaining in force, in relation to those operations, a system of internal controls which complies with best corporate governance practice as required (or, in the absence of any such requirement, recommended) by the UK listing authority (or a successor body) from time to time for listed companies in the United Kingdom.
3. Subject to the provisions of paragraph 2, nothing in this condition shall prevent:
 - (a) any affiliate in which the licensee does not hold shares or other investments from conducting any business or carrying on any activity;
 - (b) the licensee from holding shares as, or performing the supervisory or management functions of, an investor in respect of any body corporate in which it holds an interest consistent with the provisions of this licence;

- (c) the licensee from performing the supervisory or management functions of a holding company in respect of any subsidiary; or
- (d) the licensee from carrying on any business or conducting any activity to which the Authority has given its consent in writing.

4. Nothing in this condition shall prevent the licensee or an affiliate or related undertaking of the licensee in which the licensee holds shares or other investments (a **“relevant associate”**) from conducting de minimis business as defined in this paragraph so long as the limitations specified in this paragraph are complied with.

(a) For the purpose of this paragraph, **“de minimis business”** means any business or activity carried on by the licensee or a relevant associate or relevant associates other than:

- (i) the transportation business; and
- (ii) any other business activity to which the Authority has given its consent in writing in accordance with paragraph 3(d).

(b) The licensee or a relevant associate may carry on de minimis business provided that neither of the following limitations is exceeded, namely:

- (i) the aggregate turnover of all the de minimis business carried on by the licensee and the equity share of the aggregate turnover of all the de minimis business carried on by all its relevant associates does not in any period of twelve months commencing on 1 April of any year exceed 2.5 per cent of the aggregate turnover of the licensee as shown by its most recent audited historical cost accounting statements; and
- (ii) the aggregate amount (determined in accordance with sub-paragraph (d) below) of all investments made by the licensee in de minimis business, carried on by the licensee and all relevant

associates, does not at any time after the date at which this condition takes effect in this licence exceed 2.5 per cent of the sum of the share capital in issue, the share premium and the consolidated reserves (including retained earnings) of the licensee as shown by its most recent audited historical cost accounting statements.

(c) For the purpose of sub-paragraph (b) above, **“investment”** means any form of financial support or assistance given by or on behalf of the licensee for the de minimis business whether on a temporary or permanent basis and including (without limiting the generality of the foregoing) any commitment to provide any such support or assistance in the future.

(d) At any relevant time, the amount of an investment shall be the sum of:

(i) the value at which such investment was included in the audited historical cost balance sheet of the licensee as at its latest accounting reference date to have occurred prior to the date on which this condition came into effect (or, where the investment was not so included, zero);

(ii) the aggregate gross amount of all expenditure (whether of a capital or revenue nature) howsoever incurred by the licensee in respect of such investment in all completed accounting reference periods since such accounting reference date; and

(iii) all commitments and liabilities (whether actual or contingent) of the licensee relating to such investment outstanding at the end of the most recently completed accounting reference period,

less the sum of the aggregate gross amount of all income (whether of a capital or revenue nature) howsoever received by the licensee in respect of such investment in all completed accounting reference periods since the accounting reference date referred to in sub-paragraph (d)(i).

5. For the purpose of paragraph 4, “**equity share**”, in relation to any shareholding, means the nominal value of the equity shares held by the licensee in a relevant associate, as a percentage of the nominal value of the entire issued equity share capital of that relevant associate.

Condition 44. Availability of Resources

1. The licensee shall at all times act in a manner calculated to secure that it has available to itself such resources, including (without limitation) management and financial resources, personnel, fixed and moveable assets, rights, licences, consents and facilities, on such terms and with all such rights, as shall ensure that it is at all times able:
 - (a) to properly and efficiently carry on the transportation business of the licensee; and
 - (b) to comply in all respects with its obligations under this licence and such obligations under the Act as apply to those activities authorised by this licence including, without limitation, its duty to develop and maintain an efficient, co-ordinated and economical system of gas transportation.
2. The licensee shall by 31 July of each year submit to the Authority a certificate, approved by a resolution of the board of directors of the licensee and signed by a director of the licensee pursuant to that resolution, in one of the following forms:
 - (a) “After making enquiries, and having taken into account in particular (but without limitation) any dividend or other distribution which might reasonably be expected to be declared or paid by the licensee, the directors of the licensee have a reasonable expectation that the licensee will have sufficient financial resources and financial facilities available to itself to enable the licensee to carry on the activities authorised by the licence held in accordance with its obligations under the Act and such licence for a period of 12 months from the date of this certificate.”
 - (b) “After making enquiries, and having taken into account in particular (but without limitation) any dividend or other

distribution which might reasonably be expected to be declared or paid by the licensee, the directors of the licensee have a reasonable expectation, subject to what is explained below, that the licensee will have sufficient financial resources and financial facilities available to itself to enable the licensee to carry on the activities authorised by the licence held in accordance with its obligations under the Act and such licence for a period of 12 months from the date of this certificate. However, they would like to draw attention to the following factors which may cast doubt on the ability of the licensee to carry on the activities authorised by the licence held in accordance with its obligations under the Act and such licence.”

- (c) “In the opinion of the directors of the licensee, the licensee will not have sufficient financial resources and financial facilities available to itself to enable the licensee to carry on the activities authorised by the licence held in accordance with its obligations under the Act and such licence for a period of 12 months from the date of this certificate.”
3. The licensee shall submit to the Authority with that certificate a statement of the main factors which the directors of the licensee have taken into account in giving the certificate, together with a confirmation of the availability of financial facilities and a working capital statement in the format required by the UK listing authority (or a successor body) from time to time for listed companies in the United Kingdom.
 4. The statement submitted to the Authority in accordance with paragraph 3 shall be approved by a resolution of the board of directors of the licensee and must be signed by a director of the licensee pursuant to that resolution.
 5. The licensee shall inform the Authority in writing immediately if the directors of the licensee become aware of any circumstance which causes them no longer to have the reasonable expectation expressed in the most recent certificate given under paragraph 2.
 6. The licensee shall require that each certificate provided for in paragraph 2 is accompanied by a report prepared by its auditors and addressed to the Authority

stating whether or not the auditors are aware of any inconsistencies between, on the one hand, that certificate and the statement submitted with it and, on the other hand, any information which they obtained during their audit work on the most recent audited accounting statements of the licensee.

7. The directors of the licensee shall not declare or recommend a dividend, and the licensee shall not make any other form of distribution within the meaning of section 263 of the Companies Act 1985, or redeem or repurchase any share capital of the licensee unless prior to the declaration, recommendation or making of the distribution redemption or repurchase (as the case may be) the licensee has issued to the Authority a certificate complying with the following requirements of this paragraph:

- (a) The certificate shall be in the following form:

“After making enquiries, the directors of the licensee are satisfied:

- (i) that the licensee is in compliance in all material respects with all obligations imposed on it by Standard Condition 24 (Provision of Information to the Authority), Standard Condition 43 (Restriction on Activity and Financial Ring Fencing), Standard Condition 44 (Availability of Resources), Standard Condition 45 (Undertaking from Ultimate Controller), Standard Condition 46 (Credit Rating of Licensee) and Standard Condition 47 (Indebtedness) of its licence; and
- (ii) that the making of a distribution redemption or repurchase of [] on [] will not, either alone or when taken together with other circumstances reasonably foreseeable at the date of this certificate, cause the licensee to be in breach to a material extent of any of those obligations in the future”.

- (b) The certificate shall be signed by a director of the licensee and must have been approved by a resolution of the board of directors of the licensee

passed not more than 14 days before the date on which the declaration, recommendation or payment will be made.

- (c) Where the certificate has been issued in respect of the declaration or recommendation of a dividend, the licensee shall be under no obligation to issue a further certificate prior to payment of that dividend, provided that such payment is made within six months of the issuing of that certificate.

Condition 46. Credit Rating of Licensee

1. The licensee shall take all appropriate steps to ensure that the licensee maintains at all times an investment grade issuer credit rating, or with the prior written permission of the Authority, any such arrangements as the Authority considers appropriate.

2. In this condition:

“issuer credit rating” means

- (a) an issuer rating by Standard & Poor’s Ratings Group or any of its subsidiaries;
- (b) an issuer rating by Moody’s Investors Service Inc. or any of its subsidiaries;
- (c) an issuer senior unsecured debt rating by Fitch Ratings Ltd or any of its subsidiaries; or
- (d) a rating which, in the opinion of the Authority, notified in writing to the licensee, is equivalent to those referred to in sub-paragraphs (a), (b) or (c) and issued by:
 - (i) any of the credit rating agencies referred to in sub-paragraphs (a), (b) or (c) or;
 - (ii) any other reputable credit rating agency which, in the opinion of the Authority, notified in writing to the licensee, has comparable standing in both the United Kingdom and the United States of America.

In relation to any issuer credit rating, **“investment grade”** means:

- (a) unless sub-paragraph (b) below applies:

- (i) an issuer rating of not less than BBB- by Standard & Poor's Ratings Group or any of its subsidiaries;
 - (ii) an issuer rating of not less than Baa3 by Moody's Investors Service Inc. or any of its subsidiaries;
 - (iii) an issuer senior unsecured debt rating of not less than BBB- by Fitch Ratings Ltd or any of its subsidiaries; or
 - (iv) a rating which, in the opinion of the Authority, notified in writing to the licensee, is equivalent to those referred to in sub-paragraphs (i), (ii) and (iii) and issued by:
 - (aa) any of the credit rating agencies referred to in sub-paragraphs (i), (ii) or (iii); or
 - (bb) any other reputable credit rating agency which, in the opinion of the Authority, notified in writing to the licensee, has comparable standing in both the United Kingdom and the United States of America.
- (b) such higher rating as may be specified by those agencies from time to time as the lowest investment grade credit rating.

Condition 47. Indebtedness

1. In addition to the requirements of Standard Condition 29 (Disposal of Assets), the licensee shall not without the prior written consent of the Authority (following the disclosure by the licensee of all material facts):
 - (a) create or continue or permit to remain in effect any mortgage, charge, pledge, lien or other form of security or encumbrance whatsoever, undertake any indebtedness to any other person or enter into or continue or permit to remain in effect any guarantee or any obligation otherwise than:
 - (i) on an arm's length basis;
 - (ii) on normal commercial terms;
 - (iii) for a permitted purpose; and
 - (iv) (if the transaction is within the ambit of Standard Condition 29 (Disposal of Assets)) in accordance with that condition;
 - (b) transfer, lease, license or lend any sum or sums, asset, right or benefit to any affiliate or related undertaking of the licensee otherwise than by way of:

- (i) a dividend or other distribution out of distributable reserves;
 - (ii) repayment of capital;
 - (iii) payment properly due for any goods, services or assets provided on an arm's length basis and on normal commercial terms;
 - (iv) a transfer, lease, licence or loan of any sum or sums, asset, right or benefit on an arm's length basis, on normal commercial terms and made in compliance with the payment condition referred to in paragraph 2;
 - (v) repayment of or payment of interest on a loan not prohibited by sub-paragraph (a);
 - (vi) payments for group corporation tax relief or for the surrender of Advance Corporation Tax calculated on a basis not exceeding the value of the benefit received; or
 - (vii) an acquisition of shares or other investments in conformity with paragraph 2 of Standard Condition 43 (Restriction on Activity and Financial Ring fencing) made on an arm's length basis and on normal commercial terms,

provided, however, that the provisions of paragraph 3 or 4 below (as the case may be) shall prevail in any of the circumstances described or referred to therein;
- (c) enter into an agreement or incur a commitment incorporating a cross-default obligation; or
- (d) continue or permit to remain in effect any agreement or commitment incorporating a cross-default obligation subsisting at the date in which this condition came into effect, save that the licensee may permit any cross-default obligation in existence at that date to remain in effect for a period not exceeding twelve months from that date, provided that the cross-default obligation is solely referable to an instrument relating to the provision of a loan or other financial facilities granted prior to that date and the terms on which those facilities have been made available as subsisting on that date are not varied or otherwise made more onerous,

provided, however, that the provisions of sub-paragraphs (c) and (d) shall not prevent the licensee from giving any guarantee permitted by and compliant with the requirements of sub-paragraph (a).

2. The payment condition referred to in paragraph 1(b)(iv) is that the consideration due in respect of the transaction in question is paid in full when the transaction is entered into unless either:
 - (a) the counter-party to the transaction has and maintains until payment is made in full an investment grade issuer credit rating; or
 - (b) the obligations of the counter-party to the transaction are fully and unconditionally guaranteed throughout the period during which any part of the consideration remains outstanding by a guarantor which has and maintains an investment grade issuer credit rating.
3. Where the Authority has not granted permission for the use of alternative arrangements in accordance with paragraph 1 of Standard Condition 46 (Credit Rating of licensee), then except with the prior consent of the Authority, the licensee shall not enter into or complete any transaction of a type referred to or described in paragraph 1(b) save in accordance with paragraph 5, if:
 - (a) the licensee does not hold an investment grade issuer credit rating;
 - (b) where the licensee holds more than one issuer credit rating, one or more of the ratings so held is not investment grade; or
 - (c) any issuer credit rating held by the licensee is BBB- by Standard & Poor's Ratings Group or Fitch Ratings Ltd or Baa3 by Moody's Investors Service, Inc. (or such higher issuer credit rating as may be specified by any of these credit rating agencies from time to time as the lowest investment grade credit rating), or is an equivalent rating from another agency that has been notified to the licensee by the Authority as being of comparable standing for the purposes of Standard Condition 46 (Credit Rating of Licensee) and such rating:
 - (i) is on review for possible downgrade; or
 - (ii) is on Credit Watch or Rating Watch with a negative designation;or, where neither (i) nor (ii) applies:
 - (iii) the rating outlook of the licensee as specified by any credit rating agency referred to in sub-paragraph (c) which at the relevant time has assigned the lower or lowest investment grade issuer credit rating held by the licensee has been changed from stable or positive to negative.

4. Where the Authority has granted permission for the use of alternative arrangements in accordance with paragraph 1 of Standard Condition 46 (Credit Rating of Licensee), then except with the prior consent of the Authority, the licensee shall not enter into or complete any transaction of a type referred to or described in paragraph 1(b) save in accordance with paragraph 5, if the alternative arrangements for which the Authority has granted permission are not maintained in accordance with the conditions imposed by the Authority when giving written permission pursuant to paragraph 1 of Standard Condition 46 (Credit Rating of Licensee).
5. Where paragraph 3 or 4 applies, the licensee may not without the prior written consent of the Authority (following disclosure of all material facts) transfer, lease, license or lend any sum or sums, asset, right or benefit to any affiliate or related undertaking of the licensee as described or referred to in paragraph 1(b), otherwise than by way of:
 - (a) payment properly due for any goods, services or assets in relation to commitments entered into prior to the date on which the circumstances described in paragraph 3 or 4 arise, and which are provided on an arm's length basis and on normal commercial terms;
 - (b) a transfer, lease, licence or loan of any sum or sums, asset, right or benefit on an arm's length basis, on normal commercial terms and where the value of the consideration due in respect of the transaction in question is payable wholly in cash and is paid in full when the transaction is entered into;
 - (c) repayment of, or payment of interest on, a loan not prohibited by paragraph 1(a) and which was contracted prior to the date on which the circumstances in paragraph 3 or 4 arise, provided that such payment is not made earlier than the original due date for payment in accordance with its terms; and
 - (d) payments for group corporation tax relief or for the surrender of Advance Corporation Tax calculated on a basis not exceeding the value of the benefit received, provided that the payments are not made before the date on which the amounts of tax thereby relieved would otherwise have been due.
6. In this condition:

“cross-default obligation”

means a term of any agreement or arrangement whereby the licensee's liability to pay or repay any debt or other sum arises or is increased or accelerated or is capable

of arising, of increasing or of being accelerated by reason of a default (howsoever such default may be described or defined) by any person other than the licensee, unless:

- (i) that liability can arise only as the result of a default by a subsidiary of the licensee;
- (ii) the licensee holds a majority of the voting rights in that subsidiary and has the right to appoint or remove a majority of its board of directors; and
- (iii) that subsidiary carries on business only for a purpose within paragraph (a) of the definition of permitted purpose set out in Standard Condition 32 (Interpretation of Section C)

“indebtedness”

means all liabilities now or hereafter due, owing or incurred, whether actual or contingent, whether solely or jointly with any other person and whether as principal or surety, together with any interest accruing thereon and all costs, charges, penalties and expenses incurred in connection therewith.

“investment grade”

has the meaning given in paragraph 2 of Standard Condition 46 (Credit Rating of Licensee)

“issuer credit rating”

has the meaning given in paragraph 2 of Standard Condition 46 (Credit Rating of Licensee)

Schedule 2 to section 23(1)(b) Gas Act 1986 notice

**Pro forma
Notice of Statutory Objection**

In response to the statutory notice dated 23 January 2006 in respect of the above modification proposals, this notice constitutes a statutory objection to those proposals on behalf of [state full name of objecting gas transporter].

I confirm that I am duly authorised to give this notice of objection on behalf of [].

Signed

Date:

[Address for acknowledgment, preferably including email address]