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Dear Indra,

**RE: New entry arrangements for connecting to the gas distribution network**

Thank you for providing the opportunity to respond to this consultation. British Gas Trading (BGT) offers comments on the basis of being a shipper from existing GDN-connected facilities, including Wytch Farm and existing LNG storage facilities.

**Introduction and Executive Summary**

BGT has for a long time supported the view that the commercial market, with regulation only where necessary, is the best way of arriving at the most economically efficient outcome, where there is evidence that key factors including information transparency and real competitive pressures are able to shape the outcomes. On the other hand, where there is doubt about the extent to which these key factors exist, we believe that it is appropriate for regulation to play a more significant role.

We raised concerns about the treatment of GDN entry points during the National Grid GDN sales process. Having reviewed the information provided in the consultation document, our original concerns remain, and we are left with a number of serious questions about the way in which commercial arrangements could be guaranteed to operate fairly.

The gas transmission and distribution networks form a dynamic system and each GDN does not operate in isolation. In particular, we could foresee situations evolving where the arrangements between a new entry point and a GDN are open to abuse; potentially leading to a smearing of costs on to other industry players, in particular NTS shippers. We also believe that there is scope for the GDN, to which the new entry point is connected, to benefit unfairly over another GDN.

As a result of these concerns, at this stage we do not support the further development of a commercial arrangements framework for GDN entry.

Whilst we fully understand the commercial pressures, and indeed security of supply issues, that exist with respect to the Holford development, we do not consider that these pressures outweigh the primary concerns of developing an appropriate and sustainable solution. We would certainly not wish to rush through an inappropriate solution that risked setting a precedent for future developments.

The remainder of our response is set out in two parts. First, we discuss our concerns about the proposed commercial framework, and the reasons that we cannot support such an approach. Notwithstanding these objections, we secondly go on to set out our thinking on the application of a commercial framework, should our fundamental concerns be addressed.

### **Concerns relating to the commercial agreement approach**

BGT believes that there are serious implications to the whole industry of allowing potentially unfair or discriminatory arrangements to be introduced as a result of commercial negotiations between a new entry point and a GDN. Our concerns include:

- The potential for a bilateral agreement to contain conditions and charges that are opaque, and contain scope for undue discrimination.
- The competitive or financial advantage that might derive to a GDN, at the expense of others, from having an embedded storage facility attached in respect of use of capacity on a peak day.
- Interaction with the new arrangements being considered for exit, in particular a GDN's need and ability to book capacity and flexibility from the National Transmission System.
- The potential for undue delays for new projects in agreeing commercial terms (discussed later in the paper).
- Third party access: we note that no reference is made to this aspect of storage arrangements, or exemptions from such that may have been granted, and we are simply unclear how commercial arrangements could interact with third party access. It is not clear how entry capacity (firm and interruptible) would be made available and how the charging methodology for the capacity would prevent any potential cross-subsidy.
- Similarly, we are not clear how entry capacity into a GDN would be different to the NTS, and how existing holders of NTS entry capacity, which is deemed to include the GDN entry flows, would be affected.
- The lack of process for bringing any arrangements concluded bi-laterally into line with the evolving Network Code to ensure consistency.

- Prevention of a two-tier system where storage facilities attached to the NTS operate under a different commercial environment from those attached to a GDN.
- Increased complexity of differing arrangements according to location.
- The lack of overall control or visibility of arrangements:
  - where a proposed embedded storage facility may have a negative impact on neighbouring GDNs and/or NTS shippers generally, there does not seem any process for identifying and consulting relevant stakeholders to reach a solution which would maintain a fair commercial balance; and
  - where the potential for a set of commercial arrangements to appear appropriate when viewed in the context of a single GDN, but to be economically inefficient when considered in the context of the overall gas network, especially neighbouring GDNs.

In order to ensure that all arrangements between a new entry point and a GDN are seen to be fair and equitable, in addition to licence conditions, BGT believes that there would need to be complete transparency of the contract between the two parties involved. In particular, the basis for the terms and prices/charges offered by the GDN should be open to external scrutiny in order that they may be compared to obligations avoided.

Given this necessary level of transparency, we believe that a GDN will be compelled to adhere rigidly to acceptable, regulated principles when agreeing terms with a new entry point. This will remove most if not all scope for contractual creativity and innovation, with each contract effectively reflecting a “regulated” position. If this were then to be the case, it is questionable what value a commercial framework could add.

Indeed, it is BGT’s belief that a regulated approach could offer benefits in terms of certainty, and in some cases could also prove to be less time consuming, particularly in situations where more contentious new entry arrangements might require Ofgem determinations on one or more points under a commercial framework. This is an especially important consideration in the current climate of very tight supply/demand balances over the next two or three winters.

### **Protecting all Network Users under a commercial regime**

There are several classes of User of the system that may be impacted by a new connection. The most obvious is the User that wants to connect to the system, and we cover this first. It is also important to note, however, that other Users may be impacted by both the agreement directly, e.g. shippers wanting to get capacity at the new entry point, or indirectly as a result of interaction between GDNs, or a GDN and the NTS.

### **New Entry Points**

A new entry point could potentially have recourse to action under the Competition Act 1998 (CA98) where it believed that a GDN was abusing its position as the monopoly network owner. However, such action would be both extremely costly and time

consuming, and in reality these challenges could deter a small producer or storage operator from embarking upon a CA98 challenge to an unfavourable entry point decision.

We believe that useful parallels can be drawn with the competition framework in the water industry. In that industry, our understanding is that prior to the Water Act 2003, potential new entrants were required to negotiate with the incumbent network owner/operator in order to try to secure network access rights. That process took place very much against a background of CA98, with Ofwat playing a very minor role – essentially limited to ensuring that incumbents produced a network code, and acting in a dispute resolution capacity.

Under that regime, progress towards new system entry was extremely slow, successful agreements being almost non-existent. The water licensing framework did not establish a framework for equitable third party network entry arrangements, leaving the incumbent with very little incentive to agree to any new common carriage arrangements.

A similar situation must not be permitted to arise in the gas industry, and Ofgem therefore would have a number of very important roles to play, were a commercial route to be chosen. These include setting out the key principles as a framework for any new agreement, enshrining these principles within appropriate licence conditions, and determining disputes referred to it. This will ensure that new entry points are able to progress with an acceptable level of regulatory certainty, against a background of non-discrimination.

Primarily, we agree with the need for robust licence conditions upon GDNs. Whilst recognising that detailed licence condition still need to be worked up, we believe that the principles set out in the consultation document are reasonable, but in addition would suggest the following:

- Either within the licence condition or an associated document (e.g. a guidance note – see below) we would advocate a framework timetable being published. The purpose of such a document would be to prevent any undue delay on either party to the connection agreement. Such a timetable should also set out a timescale within which Ofgem would act to determine any disputes referred to it.
- The licence condition should make clear that where a GDN intends to levy charges for assessing network reinforcement and other engineering work, or indeed charges for its time in negotiating with the new entry point, the GDN should be required to publish a schedule of charges.
- The ability to refer an issue to Ofgem for determination should be open to both the new entry point and the GDN. This could avoid unnecessarily time consuming discussions where a GDN believes the expectations of a new entry point are unreasonable.

We do not believe that it will be necessary for all of this level of detail to be provided in revised GT licence conditions; it could, for example, be set out in associated guidance which both parties should adhere to as “best practice” when negotiating a new arrangement.

There could be value in Ofgem publicising any disputes that are referred to it, in order that determinations, or decisions not to provide a determination, should act as precedents for any future issues of a similar nature.

At paragraph 3.19, Ofgem sets out the principle that new GDN entry points should be offered equivalent terms to those provided to any similar existing GDN entry points. We broadly agree with this statement, providing that there is confidence that all existing entry arrangements are fair and equitable. To base new arrangements on existing, inappropriate arrangements will, of course, simply perpetuate the inequalities.

We believe that a licence condition to offer terms on a non-discriminatory basis is essential in providing some protection from such a situation arising. Further, we would advocate that such a licence condition explicitly requires that where a new entry point is required to make a financial contribution, these must be cost reflective.

### Other Relevant Stakeholders

Ofgem raises a point about whether the size of the entry point should affect the regulatory/contractual framework surrounding network entry. We do not believe that it is size *per se* that would be a differentiating factor, but rather the size of the entry point in the context of the impact on the network. For example, a very large new entry point is likely to require more careful planning, and potentially more work, in order to successfully complete. We believe that there should be sufficient transparency and consultation to be able adequately to deal with any such challenges, especially given Ofgem's role in determining disputes.

The processes governing the control and visibility of any proposed agreements should be sufficiently robust to ensure that new connections are not made to the detriment of any other industry players.

### Charging methodologies and gas trading at the NBP

Charges should clearly be cost reflective and transparent, and should recognise charges avoided by parties, e. g. Exit capacity (and Flexibility), SO Entry Commodity, SO Exit Commodity.

We do not foresee any particular challenges in ensuring that a shipper entering gas to a GDN-connected entry point is able to trade that gas at the NBP if the correct charges for services are appropriately applied.

### Existing arrangements

BGT is not aware of any specific problems relating to current arrangements for GDN entry. An absence of problems would tend to limit the urgency with which existing arrangements are timetabled for restructuring, whatever outcome is decided upon.

That said, BGT believes there will be a number of additional challenges involved in migrating existing arrangements to any new framework, including:

- Potentially significant changes to pricing and operational regimes, which could serve to render an entry point uneconomic;
- Interrupting enduring commercial arrangements, with potentially large break clause payments becoming due as a result.

We are unable to offer any specific suggestions as to how all existing entry points can be managed on to new arrangements, other than to tackle them each on a case by case basis with due regard to the principles adopted for newly connecting facilities.

I hope these comments are helpful in arriving at a conclusion, and please don't hesitate to contact me if you have any queries about this response.

Yours sincerely

Chris Wright  
**Contracts Manager**