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12th January 2007

Dear Sonia,

xoserve's response to Ofgem's Initial Proposals for National Grid Gas System Operator Incentives, ref 208/06

Thank you for the opportunity to respond to Ofgem's initial proposals for National Grid Gas System Operator Incentives. We are limiting our response to question 14 of chapter 3 concerning costs associated with future modifications to commercial frameworks.

The Industry Dialogue on xoserve Services initiated by Ofgem is making good progress. We are confident that the Work Group will recommend practical and pragmatic proposals for achieving Ofgem's objectives. Two of the key areas for discussion by the Work Group have been the high level features of UK Link and the funding of the replacement project planned for implementation in 2012.

The UK Link replacement project is an opportunity to ensure that the gas industry's central systems are fit for purpose for the gas market over the next 10-20 years. xoserve will be commencing an industry consultation exercise during 2008 to gather requirements and to facilitate industry decisions on the functionality required from UK Link so that detailed design work can commence in 2010. Any commercial regime changes that are defined in sufficient time to be included in the replacement design are likely to be significantly less costly than if added on to existing systems or the replacement system once implemented.

The Work Group has concluded that the anticipated commercial regime for 2012 onwards will have changed by 2010 when design work is due to commence, but there is insufficient time during the Industry Dialogue or definition of business requirements at this stage in order to assess a realistic implementation cost. Consequently, the Work Group has taken the view that a broadly 'as is' replacement should be funded via price control allowances, as this is predictable, with a

mechanism to recover the cost of providing additional or modified functionality as agreed with the industry during the more extensive consultation period. Only in this way can the opportunity be taken to introduce industry required changes to the commercial regime at a cost which takes advantage of the replacement work.

We support the process proposed by National Grid Gas for appropriate remuneration for developments to the commercial regime. If applied to all Networks, it is a model that could also be utilised for the funding of additional or modified functionality for the replacement of UK Link. It would provide clarity of funding and allow industry decisions to be taken with full knowledge of how any enhancements would be funded. The proposal requires full transparency and accountability to industry working groups. xoserve would fully support making the necessary information available to the industry.

We don't believe that utilising the IAE provision would provide the same level of clarity of funding and so could frustrate the development of the commercial regime.

If you have any questions or comments about what we have raised in this letter please do not hesitate to contact myself or Nick Salter. We are happy for you to publish this letter as part of the consultation process.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Jon Carlton', is centered within a light blue rectangular box.

Jon Carlton
Chief Executive Officer
xoserve Limited