



Gas Transporters and other
interested parties

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value for all customers*

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Dear Colleague

Consultation - Review of consents for Gas Transporter to Gas Transporter (GT-2-GT) services

Ofgem regulates nine price controlled Gas Transporters (GTs); the eight Gas Distribution Networks (GDNs) and the National Transmission System (NTS). Certain services provided by GTs to other GTs and Xoserve (which is jointly owned by the GTs) are currently covered by consents granted by the Authority which allow GTs to provide these services without the revenues earned in doing so contributing towards their de minimis¹ limit.

We are now reviewing the provision of those services which are currently covered by consents. This review intends to look at the following issues:

- Which services should the GTs continue to provide?
- For those services which continue to be provided by a regulated company: what is the best way to ensure compliance with the licence? Should Ofgem continue to issue consents on a case by case basis or should we sanction the ongoing provision of certain services through the licence? This may be done by adding to the list of permitted purposes or excluded services in GDNs' licences.
- Are there concerns relating to the restriction, distortion or restriction of competition arising from the provision of these services?

We invite all concerned parties to participate in this review by responding to this letter before the **29 January 2009**.

Background

As part of the sale of four of the gas distribution networks, the NTS and GDNs entered into a range of contractual agreements to provide services to each other and the Authority gave consent to these contracts in the form of an exemption to the de minimis threshold.

¹Under de minimis arrangements the licence permits the GDN to carry on a business or activity outwith its permitted purpose without seeking Ofgem's consent, provided that the annual aggregate turnover and aggregate amount of such activity does not exceed 2.5 per cent of the GDN's issued share capital or reserves at any time or 2.5 percent of overall yearly annual turnover. De minimis activity is outside the price control.

In many cases the need for consent has fallen away as contracts for the provision of services have expired or the new GDNs have either taken over the responsibility for providing or contracting out these services or contracted with another party to provide them. However, as part of the gas distribution network price control review (GDPCR) we noted that a number of these contractual agreements remained, including:

- maintenance services at offtake points;
- emergency assistance services;
- administrative services for Xoserve;
- the provision of the national emergency phone number, and;
- a number of transmission services.

These services are discussed in greater detail below. Also, National Grid Gas Distribution (NGGD) provides area control centre services to other GDNs. This is for a transitional period only, so that by the time the current consents expire each GDN group should have their own control centre, and we do not consider there is any need to include these services in this review.

Earlier this year we granted an extension to these consents. Where GDNs had proposed an expiry date for the consent we granted consent up to the date proposed. GDNs have expressed their view that certain consents should be evergreen. For these consents we set an expiry date of 31 March 2009 and determined that it would be appropriate to consult with industry participants on the options concerning the treatment of any outstanding consents beyond 31 March 2009. We also granted consent to the NTS operator, NGGT for transmission services that it provides to the GDNs. NGGT was also seeking an evergreen consent and we have extended this consent until 31 March 2009.

The aim of this review, therefore, is to consult with industry on how best to deal with those services which have, to date, been covered by consents.

There are three options for dealing with the costs of the provision of these services:

- Services could be added to the list of permitted activities/excluded services under the relevant licence condition (this is equivalent to granting evergreen consents). This option would be preferred where there is no practical prospect of another party providing these services at an efficient cost.
- GTs could be given time-limited consents – for example until the end of the current price control – to exclude the cost of the services from their de minimis limit (status quo). This option would be preferred where there is a practical prospect of another party providing these services at an efficient cost within the timeframe of the consent. This option would also allow us to make the consents conditional on particular actions by the GT. For example if we considered that it was in the interests of customers that the provision of certain services should be unbundled in order to allow third parties to compete for the provision of certain elements of those services, we could impose this condition through the consent.
- Consents could be withheld. In this case, should a licensee continue to carry out the service, costs should contribute towards their de minimis limit. If the services were being provided in a way that potentially prevented other third parties from competing to provide the service.

We note however that if either withholding of consent or proposing a conditional consent made it unattractive for the service provider to continue providing the service, there might be severe practical barriers, at least in the short term, to the provision of these services, which are essential to the safe and efficient operation of the networks.

The following section provides further detail on the contractual agreements for which the GDNs and NGGT are seeking extended or evergreen consents, and, where appropriate, our initial view on how the agreements should be treated.

Services that GDNs provide to NGG NTS

Agreement for the Provision of Offtakes and General Assets Maintenance Services

Under this agreement the GDNs provide maintenance services for NTS at certain offtake points located on the GDN's network. GDNs argue that it would be inefficient for both parties to maintain the assets. The HSE require that maintenance be carried out by competent and trained engineers. These engineers could be employed either by GDNs, by NTS or by a third party provider. Maintenance services include:

- routine maintenance – including mechanical, electrical, instrumental and telemetry
- non routine maintenance – as agreed with UK Transmission under the service agreement
- annual maintenance plan
- emergency services
- qualified resources available on reasonable endeavours basis to support NTS maintenance when requested

Ofgem's initial view is that it would be inefficient for both GDNs and NGG NTS to maintain the assets. We invite views as to how these services should be provided and on how the costs of the services should be treated.

Services that GDNs provide to each other

Emergency Assistance Agreement with other GDNs

Under this agreement the GDNs agree to lend resources to each other and to Independent Gas Transporters (IGTs) to assist in the case of a major interruption on the distribution network. This agreement is in place to deal with the aftermath of an emergency and not the emergency itself. For example this covers the assistance given in restoring gas to individual customers after an initial interruption has been dealt with, but does not include emergency services such as taking the initial call, attending the site of the emergency and making the site safe.

We consider that it is appropriate for the GDNs to continue to provide these services to ensure that customers are reconnected to the gas network in a timely manner. Traditionally this contract has been entered into as a de minimis activity with consent for exemption from the de minimis threshold. However, Standard Special Condition A41 (SSC A41) places an obligation on the licensee, if directed by the Authority, to enter into an agreement with other GTs for the provision of emergency services on behalf of that GT, including where necessary the repair of pipes where a major loss of supply has occurred.

Ofgem's initial view is that this licence obligation is not explicitly limited to dealing with the emergency itself but can include resolving the aftermath of an emergency. If the activities currently provided through the Emergency Assistance Agreement were to be included in SSC A41 then this agreement would be treated as an excluded service² in accordance with paragraph 4(a) of Special Condition E18 (Excluded Services).

² i.e. the costs are excluded from the price control

We are seeking views on whether it is appropriate to include the Emergency Assistance Agreement within the remit of SSC A41

Services that NGGD provides to other GDNs and xoserve

xoserve – General Services Agreement

NGGD provides a number of administrative services for Xoserve including:

- HR services;
- Payroll;
- P&L; and
- Communications.

The Xoserve contract was signed for a 5 year term at the time of network sales (Hive down) and will expire around May 2010.

Our initial view is that if NGGD continues to provide these services throughout the price control period we could either amend Special Condition E18 (Excluded Services) (SC E18) to include these costs as excluded services or we could extend the consent until 31 March 2013 and review whether to include these services in SC E18 as part of the next GDPCR or GDN licence review.

We are seeking views on whether it is appropriate to amend SC E18 to include the xoserve general services agreement or whether to extend the consent for this agreement until 31 March 2013 and review whether to treat this service as an excluded service as part of the next GDPCR or GDN licence review.

Agreement for the provision of call handling services

Under this agreement NGG provides a service for operating a call handling facility for the national emergency phone number. The agreement meets the current Gas Safety Management Regulations (GSMRs) requirements that there be a single point of call for all emergency enquiries.

Ofgem's current view is that GSMRs do not exclude the possibility of GDNs running separate call centres with calls channelled through a single number. **We invite views as to whether the technical challenges of call-channelling can be overcome and whether IDNs would be interested in providing this service independently. If the existing arrangement is maintained we invite views on how the costs of this service should be treated.**

Services that NGGT provides to the GDNs

Agreement for the provision of transmission services

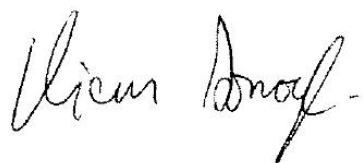
Under this agreement NTS provides a number of services to the GDNs including:

- Emergency pipeline services – standby emergency response service, making pipelines safe and repairing pipelines;
- Aerial surveillance services – over flight of pipelines and reporting on third party infringement/ encroachment
- Online inspection services – coordination of pigging activities including the provision of pigging equipment
- Specialist pipeline services – provision of specialist equipment and manpower, support to planned interventions, as requested by GDNs.

Ofgem's initial view is that, whilst there is currently nothing to stop other companies from providing these services individually, the fact that NG sells the services as a bundle may make it harder for these companies to enter the market for individual services. At the same time we recognise that bundling of the services may offer efficiency savings to customers. **We are therefore seeking views as to whether NGGT should be required to charge transmission services separately, or whether the status quo should be maintained.**

We would welcome any views on the issues set out above. We would be grateful if you could provide your comments to us by 29 January 2008. Please send your comments to Tim Bailey, Gas Distribution (Tim.bailey@ofgem.gov.uk).

Yours sincerely

A handwritten signature in black ink, appearing to read 'Kieran Donoghue'.

Kieran Donoghue

Head of Gas Distribution Regulation