

Mr. James Grayburn  
Head of RIIO-GD1  
Ofgem  
9, Millbank  
London  
SW1P 3GE

Chris Train  
Network Operations Director

Chris.Train@uk.ngrid.com  
Direct tel +44 (0)1926 655 539  
Direct fax +44 (0)1926 656 563

[www.nationalgrid.com](http://www.nationalgrid.com)

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Your Reference: Open Letter Consultation: Review of Xoserve

Dear James,

Thank you for the opportunity to input into the consultation proposed in your open letter of September 19<sup>th</sup>, 2011. National Grid Gas Transmission (NGGT) acknowledges that this consultation is being carried out as part of the RIIO-GD1 price control review of the UK's large Distribution Networks and, as a stakeholder in the services provided by Xoserve, albeit one which operates outside of the scope of RIIO-GD1, is grateful for the chance to contribute to this process.

Our reply will include specific responses to the 5 questions raised in Appendix 1 of your letter, with expansion on our views on the 3 models proposed in the CEPA report.

## Executive Summary

NGGT has reviewed the CEPA report produced in response to Ofgem's request for a review of Xoserve's Funding, Ownership and Governance and is responding to the Open Letter Consultation: "Review of Xoserve", published by Ofgem on September 19<sup>th</sup>, 2011. Our primary comments are as follows:

- We recognise that, as Transporters' Agent, Xoserve perform an essential role in the provision of central services, and have, since their inception in May 2005, been key contributors to the successful development, implementation and operation of the UK's liberalised and competitive gas market.
- We welcome the fact that Ofgem acknowledges the importance of the function performed by Xoserve, and is actively considering how this vital role is to be delivered in the future.
- We are concerned that the CEPA review and Ofgem's Open Letter Consultation do not take sufficient account of the Transmission Sector of the Gas industry, being focussed primarily on issues, views, and opinions relating to factors affecting the Gas Distribution Sector as part of RIIO-GD1.
- We do not believe that the consultation has fully considered the implications for the operation of Gemini systems or their intrinsic linkage to the strategic drivers for the Transmission industry as a whole. We are, therefore, concerned that the proposed models may negatively impact on NGGT's ability to facilitate key domestic, international, commercial

and regulatory outputs, and so will be giving consideration to whether or not the Gemini systems might be better placed to meet these challenges by delivering operational and change management of its functions internally alongside our other core systems.

- We currently believe the level of benefits each of the three proposed models will deliver do not justify their impact and cost to the industry.
- With regard to the three models proposed in CEPA's review:
  - Whilst we do not support Model A in its entirety, we consider that some elements of its proposed changes, applied incrementally, will benefit the industry as a whole, and deliver the improvements sought by Shipper representatives.
  - We do not support either Model B or Model C.
- In light of the above, we plan to engage with Ofgem's RIIO-T1 team regarding the potential impacts of changes to Xoserve's Funding, Ownership and Governance to the obligations, drivers and ambitions of the Gas Transmission industry as a whole, incorporating these into the RIIO-T1 process.

### **Question 1. Xoserve's Performance.**

**What, if any, concerns do you have with regard to the performance of Xoserve? Do you agree or disagree with CEPA's articulation of network users' concerns about the responsiveness of Xoserve to industry change, and lack of transparency (pp.28-29)?**

In commenting on Xoserve's performance, we will consider this in two parts, our experience of delivery by Xoserve in terms of Running The Business (RTB) and Change Management.

It has been our experience, and one which is reflected in Xoserve's KPI performance statistics, that Xoserve performs well in the delivery of its RTB functions. Services such as central systems operation, query handling and invoice production have, with very few exceptions, met or exceeded targets consistently since Xoserve's inception in 2005. Feedback from Shippers received as part of Xoserve's bi-annual Customer Satisfaction Survey is currently "above target" and showing an upward trend. It is our view, therefore, that little change, other than a continuation of the current trend in efficiency is required for Xoserve's RTB activities. We believe that this opinion is shared by many of Xoserve's stakeholders given the feedback received and the views expressed at the recent Ofgem meeting in which your open letter was discussed.

In terms of Xoserve's performance in the delivery of its Change Management function, we acknowledge the remarks made by some industry stakeholders in terms of operational oversight of change implementation, change costing and User Pays change as referred to in CEPA's report. Xoserve applies the PRINCE2 (PROjects IN Controlled Environments 2) structured project management method to central system change, which has been endorsed by the UK Government as the project management standard for public projects. It is our opinion that Xoserve complies with the principles of the PRINCE 2 methodology in delivering a quality change management process.

On the question of Xoserve's responsiveness to industry change, we believe that Xoserve has demonstrated a willingness and capability to provide timely and well justified system solutions to the industry. It has been our experience that many of the problems which result in stakeholder dissatisfaction with the change process are related to the way in which system / process change requirements are captured. Greater and earlier engagement with, and by, Xoserve will enable a two-way flow of information at the beginning of the change definition process. In this way, the industry has the opportunity to discuss potential options for change with Xoserve, thus leading to a more

informed, efficient and consensus-driven solution and Xoserve would also be able to exploit this earlier engagement to better assess the timeliness, priority, and cost of each change. We would also like to acknowledge recent efforts by Xoserve in this area, which has seen Xoserve representatives attending and contributing throughout the UNC change process.

Issues with the change process are often further exacerbated when the question of funding is raised. A lack of clarity and general understanding of how the User Pays funding process should be applied has, on several occasions, resulted in confusion and delay. In many cases, Xoserve has been the subject of criticism in spite of them having no decision making inputs to the User Pays funding process and, therefore, has a limited ability to influence its outcome. It is our view that a fine-tuning of the User Pays process, and hence earlier industry consideration of the costs and benefits of the change, which leads to the establishment of appropriate funding arrangements, would greatly improve the satisfaction levels with the change process.

Your letter mentions the desire for greater user involvement in the change management process and the potential creation of a Change Oversight Committee. It is our consideration that, coupled with the greater levels of engagement between the industry and Xoserve in defining business requirements and solution options, a vehicle for just such user oversight already exists in the form of the UK-Link Committee. The terms of reference for the UK-Link Committee define its role as including:

- Change delivery planning;
- Reviewing UK-Link RTB performance;
- Reviewing issues arising from UK-Link performance; and
- Reviewing changes for consistency with the UK-Link Manual.

Attempting to balance the desire for greater detail with regards to change project progress, whether in terms of time, quality or cost, against the aim of running projects efficiently and economically can lead to dissatisfaction where a stakeholder feels that insufficient levels of granularity of reporting is available. We believe that Xoserve can, with a degree of incremental change, deliver improved stage-gate level reporting to the industry. Xoserve, at the workshop hosted by Ofgem on October 24<sup>th</sup>, stated that it was willing to make these improvements, and has already begun the process with the delivery of early (Pre-ROM) High Level Estimates.

## **Question 2. Current Arrangements.**

**What concerns, if any, do you have with the current funding, governance and ownership arrangements? Do you agree or disagree with CEPA's assessment of the limitations of the current arrangements for Xoserve (pp29-32)?**

CEPA's report highlights transparency, responsiveness, speed, competitiveness and flexibility in its critique of Xoserve's operations. We agree that greater transparency should provide a greater level of understanding as to the performance and effectiveness of Xoserve's RTB and change process. We are willing to work with all industry stakeholders and Xoserve to develop these areas. In the case of Xoserve's responsiveness to change, we believe that earlier and more consistent formal engagement between Xoserve and industry stakeholders will facilitate a step change improvement in both Xoserve's actual and perceived performance in being responsive to industry needs.

Xoserve is, by virtue of its unique position as central services provider, not directly exposed to competition with other service providers. It does, however, source many of its technical change capabilities externally via a competitive tender process, thereby ensuring an efficient and economic level of service provision to its customers, both Shippers and Transporters. Xoserve's margin of 6% on the Charging Base is very competitive and reflects the risk level associated with its current funding arrangements. Private technology companies will not have the same risk profile as Xoserve and so are unlikely to be able to provide a similar service at such a discounted margin. For this reason, we believe that Xoserve delivers value for money for the suite of services it provides.

**Question 3. Options for change.**

**What are your views on the costs and benefits of the three options for change (Ch. 7)? Do you agree or disagree with CEPA's assessment of the options (Ch 8)? Are there any other options not identified by CEPA that we should consider?**

It is our view that Xoserve delivers an efficient, economic and unbiased service to the industry as a whole, with a track record since its inception which, in general, solicits praise rather than criticism. That said, we expect Xoserve to deliver continuous improvement, and so believe that there is scope for incremental change which Xoserve can achieve without having an adverse impact to the essential services it currently provides.

In terms of the 3 models proposed by CEPA, our views are as follows:

Model A – Changes within the current ownership and governance framework

We do not support Model A in its proposed form, as we feel that the impacts and costs of implementing it in full are disproportionate to the benefits it offers.

We do support increased industry stakeholder engagement in defining change requirements and setting the strategic direction of core service provision in the GB gas industry. To this end, greater involvement by all stakeholders is welcomed in terms of ensuring the most efficient and cost-effective solutions are identified and pursued in a timely way.

On the question of the extension of User Pays arrangements, we are concerned that extending the scope of the present arrangements could be premature. As stated previously, the current User Pays arrangements have proven to be divisive. The arrangements are also in their infancy with less than 3 User Pays Modification Proposals having been implemented and the costs invoiced since the arrangements were introduced. Extending these arrangements to core service areas at this time introduces a significant risk of degradation in Xoserve's ability to deliver its core function of managing and operating the central transactional systems and processes. We do, however, agree with the point made regarding the need for greater transparency with regards to the derivation of charges for User Pays services, and support the introduction of obligations on Xoserve to provide a greater level of information on its costs and a facility for the capture and resolution of issues surrounding this.

Our concerns with Model A are that it doesn't take sufficient account of the differences between the Distribution and Transmission sectors of the GB gas industry. A large part of "distribution-facing" change over the next PCR period will be driven by the implementation of Project Nexus and the roll-out of the Smart metering regime. Transmission's key strategic change over the same period, however, arises from a mix of domestic and international drivers such as Security of Supply and the

introduction of a single internal energy market within the EU. It can, therefore, be seen that the key drivers for change in the Distribution Sector arise from facilitating Shipper and end consumer service requests, whereas the drivers for change in the Transmission industry arise from extensive legislative change. This being the case, we are concerned that the Negotiated Settlement and Change Oversight functions could mean that insufficient priority is given to Transmission related regulatory-driven change, leading to issues with funding, resource availability, timely delivery and consequential impacts to NGGT's ability to meet its obligations.

#### Model B – Separate licence, customer facing GT subsidiary

In addition to the potential issues identified in Model A, the de facto "empowerment" of Xoserve to lead negotiation on behalf of the industry runs contrary to the de jure obligations, both domestic and international, placed on GTs in meeting their duties as transporters.

The way in which change is managed and resourced is different for Distribution and Transmission led initiatives, depending on whether the change is to the UK-Link suite of systems or Transmission's Gemini systems. In the former case, Distribution Sector-facing change is resourced wholly by Xoserve and its service providers. In the latter case, many of the key components of successful change management (requirements definition, process documentation, testing, etc.) are carried out by Transmission employees. The reasons for this include our need to retain skilled resource for our operational activities, the resource efficiencies enjoyed by Xoserve (and passed on to the industry) associated with the minimisation of a standing change resource pool for Gemini changes, and the annual release strategy used for Gemini implementations. Any expansion of Xoserve's control over Gemini related industry change will create resource issues for NGGT in supporting Transmission industry change, Transmission operational obligations, or both.

In general, we do not believe that the suggested magnitude of change to Xoserve's current operating model is proportionately outweighed by the benefits realised and, for this reason, do not support this model.

#### Model C – Cooperative Body

In addition to the potential issues identified with Model A, in this model, certain unspecified obligations transfer from GTs to Xoserve. Without knowing which obligations are being considered, and therefore being unable to understand how consequential hand-offs are to be managed, we cannot say at this time whether or not this proposal is appropriate. Our initial feeling is that it will be difficult to achieve a clean separation of obligations and that there is likely to be some overlap of duties leading to confusion and inefficiency. As mentioned earlier in this response, legislative changes being developed in Europe are expected to drive much of the strategic change facing the Transmission-owned Gemini Systems over the next PCR period, and it is unclear to us how the changes in obligations could accommodate both domestic and international requirements. Whilst NGGT supports an increase in stakeholder engagement in the full lifecycle of industry change, we feel that the period needed to obtain cross-industry consensus and the challenge presented in inter-distribution / transmission prioritisation, is likely to impinge on "GB plc's" ability to meet, in a timely fashion, future statutory obligations. In the case of European driven change, it is likely that we will have just 12 months to complete the full cycle of change once the European Codes have been finalised and agreed. Any move to introduce Committee-based voting on change priority and funding must be accompanied by a clear voting structure and accountability if the delivery of change is not to be negatively impacted.

We consider that the timing of this change is not ideal, given the high profile industry changes planned for the next three years, (i.e. Project Nexus, the implementation of a single internal energy market in Europe and the roll-out of Exit Reform). We believe that a move to Model C at this time is, therefore, high risk and unwarranted.

As a result of the above concerns regarding our ability to deliver appropriate and timely change to the Gemini systems, we do not support Model C.

#### **Question 4. Critical Issues**

**What are your views on the costs and benefits of the three options for change (Ch. 7)? Do you agree or disagree with CEPA's assessment of the options (Ch8)? Are there any other critical issues we should take into account before making our decision?**

The gas industry is going through a period of significant change. Market and regulatory initiatives such as Project Nexus, Smart metering, and the introduction of a single internal energy market for Europe have resulted in the placement of sizeable change programmes on Xoserve's order book. The options presented by CEPA do not appear to take into account the levels of impact of imposing each of the three paradigm shifts on the industry on Xoserve's ability to deliver its planned change programmes. It is our opinion that the magnitude of change to Xoserve's operating model is not proportionate to the benefits which could be realised and which are likely to be outweighed by the impacts to the industry in terms of meeting its strategic ambitions and statutory obligations. That said, we can see the logic in many elements of the proposed models and suggest that the following could add value:

#### Change Management / User Requirements Group

We support greater Xoserve engagement with, and by, industry participants, but believe that, rather than adding to the bureaucracy around change definition, this will be best achieved by ensuring that Xoserve is involved in the industry change process from its initial stages. Xoserve presence at UNC Modification Workgroups will enable all participants to discuss both UNC and system options for change, delivering a more informed, efficient and cost effective solution to Ofgem. As stated earlier we also recognise recent strides by Xoserve in this area.

#### Extended User Pays

As mentioned earlier, we feel that the User Pays process faces a number of challenges and is still to be fully embedded in the industry. Rather than expand the scope of a process, we believe that greater benefit could be derived from a review and simplification of the existing User Pays process, followed by a period of successful uptake by all industry participants, before consideration is given to the expansion of User Pays.

#### Negotiated Settlement

One aspect of this proposal which we support is the inclusion of the full range of industry stakeholders in the definition of requirements. We believe that this could be achieved without significant upheaval to industry governance by the earlier and increased level of stakeholder engagement with, and by, Xoserve, proposed above. Our main concern with the Negotiated Settlement proposal is the risk of causing undue delay to change programmes, especially those which are statutory or regulatory driven, thereby opening GTs up to challenges in meeting their obligations.

#### User non-executive Board member

We acknowledge that some Users have suggested that this will facilitate greater engagement in the definition of strategic change programmes. It is our experience that the Xoserve Board's primary function is to ensure the delivery of corporate governance, and that it does not get involved in the detail of individual change programmes beyond ensuring that funding has been agreed and is in place. The CEPA report suggests that some Users feel that they have limited influence over the direction and prioritisation in which change is undertaken. We believe that Xoserve's commitment to increased stakeholder engagement at all phases of the change delivery process will successfully satisfy Users' desires for greater involvement.

#### Other critical issues to be taken into account

We are concerned that this consultation was undertaken with a Distribution bias to its analysis and conclusions. Little mention has been made of the drivers affecting the Transmission industry either currently or over the next PCR period. Proposals which may have limited impact to the Distribution sector could, by reason of the lack of inclusion of Transmission industry interests in the consultation, have significant impact on the ability to achieve Transmission-related ambitions, both domestically and internationally. Therefore, we suggest that, before any step-change alterations are approved to Xoserve's Funding, Ownership and Governance, detailed consideration is given to the gas industry as a whole and input be sought from the full range of its stakeholders, both here in the UK and in Europe.

The impact of this consultation on our ability to use Gemini systems as a tool to meet our licence obligations is a concern. Elements of Gemini functionality are integral to the operation of the National Transmission System and adding additional and possibly competing layers of industry consultation could lead to undue delay to Transmission change programme delivery. It is, therefore, important for NGGT to retain the ability to specify and deliver changes to the Gemini Systems as and when required in order to satisfy its licence obligations, (including, if necessary, a re-evaluation of whether Gemini systems would be better operated and change managed internally by NGGT alongside its other core systems).

#### **Question 5**

##### **Should we change current arrangements? If so, what is your preferred option?**

NGGT believes in the principles of continuous improvement, and so supports changes where the benefits can be clearly shown to outweigh the costs / impacts. It is our view that the current model under which Xoserve operates is fit for purpose, but we agree that there are certain areas where incremental change could deliver significant benefit. These have been described earlier in this note, and are:

- Greater, and earlier, engagement between both Xoserve and the industry;
- Greater transparency of costs for both RTB and change elements of Xoserve's services.

## **In conclusion**

We are unable to support either Models A, B or C in full due to the risks they pose to the strategic interests of the Transmission industry. Whilst we accept that Model A has options for change which can add value, we believe that improvements can be achieved by the introduction of incremental alterations to the current industry change process. We feel that the consultation has not taken sufficient account of the growing delineation between Transmission and Distribution sectors, and hence the options which this delineation presents. We intend, therefore, to carry out further consideration of the various Xoserve models, taking into account the obligations, drivers and ambitions of the Transmission industry as a whole and, in discussion with Ofgem's RIIO-T1 team, incorporate these into the RIIO-T1 process.

If you would like to discuss the content of this letter at any time, please do not hesitate to contact Seán Mc Goldrick, ([Sean.J.McGoldrick@uk.ngrid.com](mailto:Sean.J.McGoldrick@uk.ngrid.com)), our Change & Contract Manager responsible for NGGT's interface with Xoserve.

Yours sincerely,



Chris Train  
Network Operations Director  
National Grid