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Dear Ian,

Formal proposals to modify the ring fence conditions in network operator licences

National Grid owns and operates the high voltage electricity transmission system in England and Wales and, as National Electricity Transmission System Operator (NETSO), operates the high voltage transmission system throughout Great Britain and offshore. National Grid also owns and operates the gas transmission system throughout Great Britain (NTS) and, through our gas distribution business, distributes gas to approximately 11 million offices, schools and homes in England.

National Grid would be subject to the proposed modifications to the “ring-fence” conditions in its electricity transmission licence and in its two gas transporter licences in respect of the NTS and gas distribution networks it owns, if these changes are implemented as currently drafted. National Grid therefore welcomes the opportunity to respond to these formal proposals.

This response is not confidential.

Proposed New Licence Condition – Sufficiently Independent Directors

National Grid continues to believe that the proposed new licence condition concerning board composition has not been shown to be needed or justified, for the reasons that have been set out in our previous consultation responses¹.

The formal consultation dated 17 December 2012 does not attempt to address these reasons on the grounds that Ofgem “*do not believe that any new points of principle arose from the most recent consultation ...*”. We do not propose to repeat the comments we have previously made in relation to the proposed new licence condition and instead refer Ofgem back to our earlier consultation responses. We urge Ofgem to consider again the lack of justification for the proposed new licence condition before directing this licence modification.

¹ See our letters dated 23 April 2010, 10 November 2010, 30 June 2011, 31 August 2012 and 30 November 2012 in response to previous consultations on this proposal.

Comments on other formal proposals to modify the ring fence conditions

We have only commented on the conditions that are applicable to the National Grid companies. However, these comments apply equally to equivalent conditions (for example the offshore electricity conditions and the gas standard conditions, which are switched off in our licences).

As explained in our previous consultation response of 31 August 2012, with the exception of the proposed new “Requirement for Sufficiently Independent Directors” condition we consider the proposed changes are generally consistent with the stated objectives and appear to enhance the internal consistency of the ring fence regime. However, there still remain some detailed drafting comments that need to be taken into consideration. We have therefore attached at Appendix 1 a table with detailed comments and suggested alternative drafting. We request that these are implemented in the conditions if the modifications are to be directed.

Other matters

Under “Other matters” on page 4, the formal consultation says that *“In addition, one respondent suggested that there should be a specific price control mechanism to reimburse the costs associated with a requirement for sufficiently independent directors. We have stated that efficient costs should be recoverable on a net present value neutral basis, but **consider that the mechanism for this should be considered under relevant price control review arrangements.**”* (emphasis added). However, the RIIO-T1 and RIIO-GD1 licence drafting that was published in late December 2012 does not appear to provide for recovery of these costs.

Therefore, consistent with the re-stated commitment to fund the costs associated with this new licence condition, for those licensees for which it is implemented an extra item should be added to the pass-through cost term PT_i (as defined at Para 3B.3 for the electricity transmission licence drafting, and in the equivalent paragraphs 2B.3 of the NTS Gas Transporter and 1C.3 of the GDN Gas Transporter licence drafting), where this extra item should be defined as *“the costs incurred by the licensee in complying with any requirements arising from compliance with the new licence condition “Requirement for sufficiently independent directors”.”*

Yours sincerely

[By e-mail]

Paul Whittaker
Director, UK Regulation

Appendix 1

Table of detailed comments

No.	Condition number	Condition name	Paragraph Ref	Comments	Suggested alternative drafting (underlined or struckthrough wherever possible)
1.	General comment			In the opening notice to the changes proposed for the gas transporter standard licence conditions 29, 44, 45, 46 and 47, Paragraph 4(f) refers to Standard Licence Condition 41: is this intended to refer to Standard Licence Condition 47 instead?	
2.	General comment			As suggested at footnote 3 of your letter dated 17 December 2012, any references to any other conditions within any of the proposed amended ring fence conditions should be checked for consistency against the re-numbered licence conditions under the RIIO-T1 and RIIO-GD1 Final Proposals licence drafting. For example, paragraph 4(b) in the proposed gas transporter Standard Special Condition A42 refers to Standard Special Condition A32 " <i>Definition of Permitted Purpose</i> ", but it is now envisaged that this definition will instead appear in Standard Special Condition A3 " <i>Definitions and interpretation</i> ".	
Electricity Transmission Licence					
3.	B3	Disposal of relevant assets	6		" <i>Receivable</i> " and " <i>Receivables</i> " should be in lower case.
4.	B3	Disposal of relevant assets	6(b)	The word " <i>clear</i> " had previously been changed to " <i>repay</i> " in order to clarify its meaning, but has now been changed back to " <i>clear</i> " without it being explained why this	

				change has been reversed.	
5.	B7	Availability of Resources	6(a)	Insert comma.	<i>"After making enquiries the licensee's directors consider that, at the time of their approval..."</i>
6.	B7	Availability of Resources	7(a), line 3		<i>"paragraph" should be "paragraphs".</i>
7.	B7	Availability of Resources	7(b), line 3		<i>"in <u>the</u> form of Certificate 3F"</i>
8.	B7	Availability of Resources	13 (and the equivalent offshore TO licence condition E8 paragraph 16)	<p>The words "<i>at all times</i>" in relation to the maintenance of the intervention plan should be deleted, consistent with the corresponding latest amended electricity distribution standard licence condition 30 and with the intent expressed at the third bullet of paragraph 2.7 in your 11th October 2012 consultation (Ref 129/2012).</p> <p>The paragraph should include the words underlined as in the corresponding electricity distribution standard licence condition 30.</p>	<i>"The licensee must prepare by 1 April 2014, <u>or within 12 months of this condition coming into effect in respect of the licensee, whichever is the later</u>, and at all times thereafter maintain..."</i>
9.	B7	Availability of Resources	13 and 14		<i>"Intervention Plan" and "Paragraph" should be in lower case to ensure consistent use of capitals and consistency with definitions.</i>
10.	B9	Indebtedness	1, line 2 1(a)(iv), line 3		<i>"Receivables" should be in lower case for consistency.</i>
11.	B9	Indebtedness	6	Reference is made to credit ratings from different named agencies (Standard and Poor's, Moody's, and Fitch), and a reference to DBRS has now been proposed. The proposed text does not refer to any affiliates or subsidiaries of the other agencies, and so, for consistency, we have proposed an amendment to the wording.	<i>"or BBB (low) by DBRS Ratings Limited or any of its affiliates"</i>

12.	B9	Indebtedness	8, after (a) and (b) and in (c)		"Writing" should be in lower case.
13.	A1	Definitions and interpretation	Definition of "investment grade" at (a)(i) Definition of "issuer credit rating" at (a)		"Standard and Poor's".
14.	A1	Definitions and interpretation	"investment grade" "issuer credit rating"	Reference is made in the definitions to credit ratings from different named agencies (Standard and Poor's, Moody's, and Fitch), and a reference to DBRS has now been proposed. The proposed text refers to "DBRS Ratings Limited or any of its affiliates", whereas ratings from the other named agencies refer to "[XXXXX] or any of its subsidiaries". In relation to DBRS the conditions should, for consistency with the other three agencies named, follow the suggested alternative drafting.	"by DBRS Ratings Limited or any of its <u>subsidiaries affiliates</u> "
15.	B22	Requirement for sufficiently independent directors	4(b)		"(as that term is defined in Standard Condition A1 (<u>Definitions and interpretation for the standard conditions</u>)))"
16.	B22	Requirement for sufficiently independent directors	12, definition of "common control company"		"(applying the definition set out in Standard Condition A1 (<u>Definitions and interpretation for the standard conditions</u>)))"
17.	B22	Requirement for sufficiently independent directors	12	Insert full stop at the end of the definition.	"participating interest" has the meaning given in section 421A of the Financial Services and Markets Act 2000_
Gas Transporter Licence					
18.	A27	Disposal of assets	7		"Receivable" and "Receivables" should be in lower case to ensure consistency with the definition.

19.	A27	Disposal of assets	7(b)	The word “ <i>clear</i> ” had previously been changed to “ <i>repay</i> ” in order to clarify its meaning, but has now been changed back to “ <i>clear</i> ” without it being explained why this change has been reversed. (This same comment applies to the proposed revised standard licence condition 29 paragraph 6(b).)	
20.	A27	Disposal of assets	9, first line	Reference should also be made to paragraph 4, as drafted in the electricity transmission licence.	<i>“Notwithstanding paragraphs 1, and 2 and 4”</i>
21.	A37	Availability of resources	7(a), third line		<i>“<u>paragraphs</u>”</i>
22.	A37	Availability of resources	7(b), second line		<i>“<u>in the</u> form of Certificate 3F”</i>
23.	A37	Availability of resources	8, second line		It looks like there is an extra space after “ <i>and</i> ”. This should be deleted.
24.	A37	Availability of resources	13	The words “ <i>at all times</i> ” in the second line in relation to the maintenance of the intervention plan should be deleted, consistent with the corresponding latest amended electricity distribution standard licence condition 30 and with the intent expressed at the third bullet of paragraph 2.7 in your 11 th October 2012 consultation (Ref 129/2012).	<i>“<u>whichever is the later</u>, and at all times thereafter, maintain...”</i>
25.	A37	Availability of resources	13, line 4		<i>“<u>Paragraph</u>”</i> should be in lower case.
26.	A37	Availability of resources	14, first line		<i>“<u>The requirement for the information described in any of sub-paragraphs (a) to (k) in the definition of intervention plan in paragraph 16 below...</u>”</i>
27.	A37	Availability of resources	16, definition of “ <i>participating owner</i> ”		<i>“Associate”</i> and <i>“Participating Owner”</i> should be in lower case for consistency with the defined terms.

28.	A38	Credit Rating of the Licensee	2, definition of “ <i>issuer credit rating</i> ” Definition of “ <i>investment grade</i> ”	Reference is made in the definitions of “issuer credit rating” and “investment grade” to credit ratings from different named agencies (Standard and Poor’s, Moody’s, and Fitch), and a reference to DBRS has now been proposed. The proposed text refers to “ <i>DBRS Ratings Limited or any of its affiliates</i> ”, whereas ratings from the other named agencies refer to “ <i>XXXXX or any of its subsidiaries</i> ”. In relation to DBRS the conditions should, for consistency with the other three agencies named, follow the suggested alternative drafting.	“by DBRS Ratings Limited or any of its <u>subsidiaries affiliates</u> ”
29.	A39	Indebtedness	1(b)(vi)	The wording should be changed to match that for the corresponding paragraph 1(b)(vi) of the electricity transmission standard licence condition B9 “ <i>Indebtedness</i> ”.	“(vi) <i>payments for group corporation tax relief or for the <u>surrender thereof</u> calculated on a basis not exceeding the value of the benefit received; or...</i> ”
30.	A39	Indebtedness	6, line 3	Reference is made to credit ratings from different named agencies (Standard and Poor’s, Moody’s, and Fitch), and a reference to DBRS has now been proposed. The proposed text does not refer to any affiliates or subsidiaries of the other agencies, and so, for consistency, we have proposed an amendment to the wording.	“or BBB (low) by <i>DBRS Ratings Limited</i> or any of its affiliates ”
31.	A39	Indebtedness	6(c), line 2	Suggested amendment for clarity.	“ <i>the rating outlook of the licensee as specified by any credit rating agency referred to in <u>this paragraph 6</u></i> ”
32.	A39	Indebtedness	9, second line		“ <i>entering into or completing <u>any</u> and transaction of a type referred to</i> ”
33.	A39	Indebtedness	9(d)	The wording should be changed to match that of the corresponding paragraph 9(d) of the electricity transmission standard licence condition B9 “ <i>Indebtedness</i> ”.	“ <i>payments for group corporation tax relief <u>or the surrender thereof</u> calculated on a basis not exceeding the value...</i> ”

34.	A39	Indebtedness	10, definition of “ <i>common control company</i> ”		“ <i>Ultimate Controller</i> ” should be in lower case for consistency with the definition.
35.	A39	Indebtedness	10, definition of “ <i>cross default obligation</i> ”	The reference in sub-paragraph (iii) to Standard Special Condition A32 will need updating following the RIIO proposed drafting to move the definition of permitted purpose to Standard Special Condition A3.	
36.	A39	Indebtedness	10, definition of “ <i>participating owner</i> ”		“ <i>Associate</i> ” should be in lower case for consistency with the definition.
37.	A42	Requirement for sufficiently independent directors	4(b)	The reference to Standard Special Condition A32 will need updating following the RIIO proposed drafting to move the definition of permitted purpose to Standard Special Condition A3.	
38.	A42	Requirement for sufficiently independent directors	13, definition of “ <i>participating interest</i> ”		Definition should have a full stop at the end.
39.	C1	Amendments to Standard Special Conditions relating to LNG	7(a) and 7(b)		The references should be to paragraph 12 rather than paragraph 13.
40.	C1	Amendments to Standard Special Conditions relating to LNG	7(c)		The reference should be to paragraph 13 rather than paragraph 14.
41.	C1	Amendments to Standard Special Conditions relating to LNG	7(c)		The paragraph numbered 14 to be inserted in Standard Special Condition A27 should be renumbered as 13. The references in lines 5 and 6 of that paragraph should be to paragraph 12 rather than paragraph 13.
42.	C1	General		It should be noted that separate sets of	

		comment		changes have been proposed to the condition in parallel, in relation to (i) this ring fence consultation and (ii) the drafting changes relating to the RIIO Final Proposals. These two sets of changes will both be needed and they will need to be implemented in such a way that they work together with no unintended interactions or effects.	
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