



Promoting choice and value for
all gas and electricity customers

To independent gas transporters and other network operators, generators, shippers, suppliers, consumers and their representatives, the sustainable development community, investors and other interested parties.

11 November 2014

Dear Colleague,

Proposal to modify Standard Licence Condition 30 (Regulatory Accounts) of the Gas Transporters Licence and make consequential modifications to Standard Licence Condition 1 (Definitions), Standard Licence Condition 44 (Availability of Resources) and Standard Licence Condition 30A (Change of Financial Year)

This letter seeks views on our proposal to modify Standard Licence Condition 30 (Regulatory Accounts) ("SLC 30") of the Gas Transporters Licence. SLC 30 is applicable to independent gas transporters ("IGTs") who own and operate relatively small gas distribution network embedded in the larger networks operated by incumbent gas distribution network operators ("GDNs"). SLC 30 is not applicable to GDNs or to the national transmission system ("NTS") licensee.

Our proposal would remove the requirement for (IGTs) to submit regulatory accounts, and make consequential modifications to Standard licence Conditions 1 (Definitions), Standard Licence Condition 44 (Availability of Resources) and Standard Licence Condition 30A (Change of Financial Year) in IGT licences.

Our proposed change to SLC 30 would align the *accounts* requirements for IGTs with the requirements applicable to independent electricity distribution network operators (IDNOs)¹ and would be consistent with the requirements of Article 31 of Directive 2009/73/EC of the European Parliament and of the Council ("the directive"). Further background information is available in Appendix 1 to this letter.

Objectives

The proposed modifications would:

- require all IGTs, regardless of their ownership structure or legal form, to file and publish audited annual accounts as if they were subject to the requirements of the Companies Act 2006;
- require IGTs to keep a copy of their audited annual accounts at the disposal of the public at their principal place of business;

¹ See Standard licence Condition 31A in the electricity distribution licence,

- remove the requirement for IGTs to submit separate audited regulatory accounts, including current cost accounts aligned to the 'formula years' referred to in Standard Special Condition A5 of the gas transporter licence; and
- require the licensee to:
 - keep separate internal accounts (records) for different segments of its business; and
 - ensure that agreed upon audit procedures are carried out by an appropriate auditor in relation to the obligation on the licensee, contained in the directive, to avoid discrimination and cross-subsidies,
 in cases where it has vertically integrated operations².

Background

SLC 30, in its current form, was drafted with regard to gas transporter licensees whose revenue is subject to formal price controls. It provides for licensees to submit regulatory accounts with a year-end aligned to the 'formula year' referred to in price control licence conditions. However, as mentioned above, SLC 30 is switched off for the NTS and GDN licensees who are instead subject to Standard Special Condition A30 (Regulatory Accounts).

Based upon recent developments in European legislation and having regard to the equivalent reporting requirements now applicable to IDNOs, we consider that SLC 30 can be usefully reformed for IGTs.

The reasons for our proposal are:

- to ensure that the requirements for the preparation, submission and availability of accounts by IGTs are fully consistent with the directive;
- to remove the requirement for IGTs to prepare regulatory accounts for the 'formula years' referred to in gas distribution price controls since IGTs are not directly subject to those price controls; and
- to bring the requirements for the preparation, submission and availability of accounts by IGTs into line with the equivalent requirements for IDNOs.

The effects of the proposed changes would be:

- to remove the requirement for IGTs to prepare and have separate regulatory accounts in addition to those required under companies legislation; and
- to require each IGT, whatever its legal form, to:
 - a. prepare accounts in accordance with the requirements of the Companies Act 2006;
 - b. retain a copy of its accounts at the disposal of the public at its principal place of business;
 - c. keep separate internal accounts for different segments of business and
 - d. arrange for agreed upon audit procedures to be carried out in relation to the avoidance of discrimination and cross-subsidies, in cases where it has vertically integrated operations.

² Meaning generation and/or energy retail activities as well as distribution activities.

Next steps

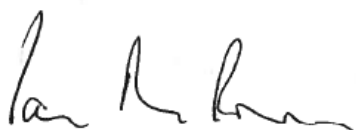
We would welcome the views of stakeholders, particularly IGTs, on the possible changes to the gas transporters licence we have outlined above. Responses should be received by 16 January 2015 and should be sent to sean.hennity@ofgem.gov.uk.

Unless marked confidential, all responses will be published in our library and on our website, www.ofgem.gov.uk. You may request that your response be kept confidential. We will respect this request, unless the law requires us to disclose anything, for example under the Freedom of Information Act 2000 or the Environmental Information Regulations 2004. If you'd like your response to remain confidential, clearly mark the document to that effect and include the reasons for confidentiality. Put any confidential material in the appendices to your response.

If we decide to proceed with formal modification proposals we will issue a statutory consultation Notice that will be open for responses for a minimum of 28 days. After considering responses, we may make changes to the licence, which will take effect not less than 56 days after the publication of our decision.

If you have any queries on the, matters referred to in this letter please feel free to contact Ofgem's Regulatory Finance team (<mailto:regulatoryfinance@ofgem.gov.uk>).

Yours faithfully



Ian Rowson
Associate Partner, Regulatory Finance

Appendix 1 – Draft of possible changes to licence conditions

Condition 30: Regulatory Accounts

The proposed change would be to delete all of the text in the existing condition and replace with the wording below.

Condition 30: Accounts

Preparation and availability of accounts

1. The licensee shall draw up, submit to audit and publish its annual accounts in accordance with any obligations to which it is subject under national company law.
2. To the extent that the licensee is not subject to an obligation to draw up and submit to audit annual accounts under national company law, the licensee shall draw up, submit to audit and publish its annual accounts as if it were a limited liability company within the meaning of sections 1 and 3 of the Companies Act 2006.
3. The licensee shall keep a copy of its annual accounts at the disposal of the public at its principal place of business.

Internal accounting

4. The licensee, in its internal accounting, shall:
 - (a) keep separate accounts for any gas distribution, transmission and storage activities it carries out, as if such activities were carried out by separate undertakings, to avoid discrimination, cross-subsidisation and the distortion of competition; and
 - (b) keep consolidated accounts for other activities not relating to gas transportation, in each case, sufficient to allow for the preparation of a balance sheet and a profit and loss account for the activity or set of activities concerned.

Audit requirement

5. Subject to paragraph 7, the licensee must, at its own expense, enter into a contract of appointment with an appropriate auditor for the completion of agreed upon procedures in relation to the prohibition of cross-subsidies and discrimination contained in paragraph 3 of Article 31 of Directive 2009/73/EC of the European Parliament and the European Council of 13 July 2009 ("the directive").
 6. The contract of appointment referred to in paragraph 5 must provide for the appropriate auditor to:
 - (a) carry out agreed upon procedures in relation to each financial year; and
 - (b) address a report to the Authority by 31 July following the end of each financial year which:
 - (i) states that they have completed the agreed upon procedures in a manner consistent with relevant auditing standards; and
 - (ii) sets out their findings in respect of the financial year under report.
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7. The licensee need not enter into the contract of appointment referred to in paragraph 5 in respect of a particular financial year provided that:
- (a) during the whole of that financial year it does not carry out any gas transmission or storage activities;
 - (b) during the whole of that financial year, none of its associates is a relevant electricity undertaking or a relevant natural gas undertaking; and
 - (c) by 31 July following the end of the financial year, it submits to the Authority a certificate that has been signed by a director of the licensee and includes the following wording:

“During the last financial year the licensee has not carried out any gas transmission or storage activities, and none of the licensee’s associates (within the meaning of the definition given in Standard Condition 30 of the gas transporters licence) (“SLC 30”) has been a relevant electricity undertaking or a relevant natural gas undertaking (within the meanings of the definitions of those terms given in SLC 30).”

8. If the Authority is satisfied, with respect to a particular financial year, either:
- (a) that the report referred to in paragraph 6(b) demonstrates that the licensee has complied with the obligation to avoid discrimination and cross-subsidies that is referred to in paragraph 3 of Article 31 of the directive; or
 - (b) that the certificate referred to in paragraph 7(c) confirms that the licensee has not carried out any gas transmission or storage activities and that none of the licensee’s associates has been a relevant electricity undertaking or a relevant natural gas undertaking,

then the audit requirement referred to in paragraph 4 of Article 31 of the directive will be deemed to have been met.

Interpretation

9. In this condition:

“agreed upon procedures” means procedures from time to time agreed between the Authority, the appropriate auditor and the licensee for the purpose of enabling the appropriate auditor to review and report to the Authority on matters relating to the licensee’s compliance with the obligation to avoid discrimination and cross-subsidies set out in Article 31 of the directive.

“appropriate auditor” means:

- (a) in the case of a licensee that is a company within the meaning of section 1 of the Companies Act 2006 a person appointed as auditor under Chapter 2 of Part 16 of that Act;
- (b) in the case of any other licensee

that is required by the law of a country or territory within the European Economic Area to appoint an auditor under provisions analogous to those of Chapter 2 of Part 16 of the Companies Act 2006, a person so appointed; and

- (c) in any other case a person who is eligible for appointment as a company auditor under Part 42 of the Companies Act 2006.

“associate”

means:

- (a) an affiliate or related undertaking of the licensee;
- (b) an ultimate controller of the licensee;
- (c) a participating owner of the licensee; or
- (d) a common control company.

“common control company”

means any company, any of whose ultimate controllers (applying the definition set out in Standard Condition 1 (Definitions and Interpretation) but substituting that company for the licensee) is also an ultimate controller of the licensee.

“national company law”

means:

- (a) in the case of a licensee that is a company within the meaning of section 1 of the Companies Act 2006, that Act; and
- (b) in the case of any other licensee that is required by the law of a country or territory within the European Economic Area to comply with obligations to draw up, audit and publish annual accounts, that law.

“relevant electricity undertaking”

means a natural or legal person carrying out one or more of the following functions:

- (a) the generation of electricity;
- (b) the transmission of electricity; and
- (c) the supply of electricity.

“relevant natural gas

means a natural or legal person carrying

undertaking”

out one or more of the following functions:

- (a) the production of natural gas including LNG;
- (b) the transmission of natural gas including LNG;
- (c) the supply of natural gas including LNG; and
- (d) the storage of natural gas including LNG.

“the directive”

has the meaning given in paragraph 5 of this condition.

Condition 1: Definitions and interpretation

The proposed change is to delete the text shown crossed out below:

~~“alternative accounting rules”~~ ~~for the purposes of standard condition 30 (Regulatory Accounts) only, has the meaning given in that condition;~~

~~“consolidated transportation business”~~ ~~for the purposes of standard condition 30 (Regulatory Accounts) only, has the meaning given in that condition;~~

~~“current cost assets”~~ ~~for the purposes of standard condition 30 (Regulatory Accounts) only, has the meaning given in that condition;~~

“financial year” means, ~~subject to standard condition 30A (Change of Financial Year) (where applicable),~~ a period of 12 months beginning on 1st April of each year and ending on 31st March of the following calendar year;

~~“regulatory accounts”~~ ~~for the purposes of standard condition 30 (Regulatory Accounts) only, has the meaning given in that condition;~~

~~“the handbook”~~ ~~for the purposes of standard condition 30 (Regulatory Accounts) only, has the meaning given in that condition;~~

Standard Condition 44 (Availability of Resources)

The proposed change is to delete the text shown crossed out below

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Statement of factors and report by auditors in relation to financial resources certificate

3. The licensee must ensure that the certificate given to the Authority under paragraph 2 is accompanied by:
 - (a) a statement of the main factors that the licensee's directors have taken into account in giving that certificate including reference to:
 - (i) the main financial resources and financial facilities available to the licensee; and
 - (ii) the most recent cash flow statement prepared for the licensee;
 - and
 - (b) a report prepared by its auditors and addressed to the Authority which states whether or not the auditors are aware of any inconsistencies between, on the one hand, that certificate and the statement submitted with it under sub-paragraph (a) and, on the other hand, any information that they obtained during their audit work ~~under Standard Condition A30 (Regulatory Accounts)~~ on the licensee's ~~Regulatory Accounts~~.

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Standard Condition 30A (Change of Financial Year)

The proposed change is to delete all of the existing text in this condition and replace it with the text shown below.

1. Not in use.