



Making a positive difference
for energy consumers

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Dear Angus,

Decision to approve changes to Scotia Gas Network's Gas Network Innovation Competition project - Opening up the Gas Market

This letter contains our¹ decision to approve the change request for Scotia Gas Networks (SGN) Gas Network Innovation Competition (Gas NIC) project, Opening up the Gas Market (OUGM).

We have approved this change because we think it is in the best interests of customers and consistent with our principal objective under the Gas Act 1986 and our general statutory duties. The change will allow the project to continue to deliver value for money to customers.

Background

On 19 December 2013, we issued a Project Direction² to SGN. The Project Direction contains the terms to be complied with by the project as conditions of it being funded under the Gas NIC.

Part of the project involves injecting gas which is not currently compliant with the requirements of the Gas Safety Management Regulations 1996 (GS(M)R) into the Oban network. Clause 9 of the Project Direction states that SGN must secure an exemption from the Health and Safety Executive (HSE) allowing SGN to inject non-GS(M)R compliant gas into the network before starting stages 2 and 3 of the project. Stage 2 of the project would involve the testing of all gas appliances in Oban and stage 3 would test non-GS(M)R compliant gas in the whole Oban gas network.

Change request

In July 2014, SGN requested a change to the wording of Clause 9 of the Project Direction to allow access to funds for stages 2 and 3 of the project prior to securing the exemption from the HSE. SGN said that following engagement with HSE it has been identified that the exemption would only be granted during stage 2 of the project rather than at the end of stage 1. The HSE has explained to SGN that, in order to grant the exemption, it requires evidence gathered from the testing of a representative sample of properties in Oban.

¹ The terms "the Authority", "Ofgem", "we", "us" and "our" are used interchangeably in this letter. The Authority is the Gas and Electricity Markets Authority. Ofgem is the office of the Authority.

² Terms not defined in this document shall have the meaning given to them in the Gas NIC Governance Document.

SGN suggested that the new requirement could be to secure "an agreement in principle" from the HSE for the granting of an exemption from the obligation to comply with relevant provisions of the GS(M)R. This would mean a pre-agreed process whereby the HSE provides terms with which SGN is required to comply in order to secure the exemption. Initially the change request was to allow SGN to access £1,465,000 from the Project Bank Account to conduct stage 2 and 3 activities.

We were concerned about how customers would be protected against the risk of stranded costs if the exemption is not granted, as more of the project budget would be spent ahead of the exemption. SGN explained that the testing in stage 2 would be separated into six phases with a stage gate after each phase to assess the benefits of moving forward or not (a map showing the testing phases is included in SGN's change request³).

SGN agreed with the HSE that the best approach to securing the exemption is to carry out enough tests so that the in situ data gathered is statistically significant. DNVGL (as project partner) calculated that a representative sample of the total properties in Oban would be reached after phases 1 - 3 of the testing. Therefore SGN plans to submit the exemption request to HSE following the completion of testing in phases 1 -3 and gathering enough information to form the evidence base. As SGN is confident that the evidence from phases 1-3 will provide a strong enough case for the exemption to be granted we decided to only allow access to funds to cover those activities. Releasing the funds for only phases 1-3 will minimise the risk to customers.

The requirements with which SGN has to comply in order to secure the exemption from the HSE are not specific. We were concerned that the lack of confirmation from the HSE on the specific requirements with which SGN needs to comply could mean that SGN conducts further work but the exemption is not ultimately granted. SGN has been engaging with HSE and is confident that there is a high probability of the exemption being granted during stage 2. The evidence from the appliance tests and laboratory tests will help SGN demonstrate that the risks arising from the trial are adequately controlled and therefore strengthen the case for an exemption being granted.

To further minimise the risk to customers, if the exemption from the HSE is not secured because the HSE does not consider SGN's approach or sample to be robust, we may re-examine the appropriateness of the use of the funding released for stage 2 of the project and if deemed inappropriate, make use of the Funding Return Mechanism. SGN has also agreed to pay for the gas chromatograph ahead of the exemption being granted. If the exemption is not secured then this cost will be borne by SGN, not customers.

Decision

Following further questions to and discussions with SGN, on 17 October 2014 SGN submitted the final version of the change request. We have decided to approve this change request based on the wording set out in appendix 1 to this letter. SGN will have access to £595,000 from the Project Bank Account to undertake the stage 2 tasks (phase 1-3) and £15,000 for stage 3 tasks necessary to take place prior to securing the HSE exemption. The gas chromatograph will be purchased separately by SGN and will be reimbursed if the HSE exemption is secured.

We are satisfied that the risk to customers associated with this change have been mitigated. We think this change is in the best interest of customers as it will allow the project to continue and achieve its objectives. This change will allow SGN to complete the necessary testing required to secure the HSE exemption and to deliver considerable learning of value to network licensees and other parties. By approving this change we are not making an evaluation of SGN's overall management of the project.

³ The change request document has been published alongside this decision letter.

We note that in the change request document SGN stated that there is a significant level of learning that will be achieved in this phase of the project (as set out in pages 6-9 of its change request). It is important that SGN ensure this learning is properly captured and disseminated. We understand this will have broad value including for informing any future HSE exemptions.

We acknowledge that the delay to the project caused by this change request has impacted the overall project timeline and the dates for the Successful Delivery Reward Criteria (SCRCs). SGN has updated the SDRC dates to reflect this delay (Appendix 2). An updated project plan is included in SGN's change request.

In accordance with Section 15 of the Project Direction, we hereby amend the Schedule to the Project Direction in the manner set out in the Schedule to this letter.

This letter constitutes notice of reasons for our decision pursuant to section 38A of the Gas Act 1986.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'D. Guzeleva', with a long horizontal flourish extending to the right.

Dora Guzeleva
Head of Networks Policy, Local Grids
For and on behalf of the Authority

Appendix 1: Clause 9 with proposed amendments

The Funding Licensee must, prior to starting the activities of Stage 2 and 3 as described in the Full Submission, secure agreement in principle from the Health and Safety Executive for the necessary exemption from the Gas Safety (Management) Regulations for injecting higher Wobbe Index gas into the Oban gas network.

The Funding Licensee may access £351,000 from the Project Bank Account to undertake the Stage 1 tasks associated with securing the HSE exemption. This funding is limited to the following:

- i. Stage 1.1 – review of previous studies (up to £15,000 may be spent);
- ii. Stage 1.2 – detailed appliance population survey (up to £155,000 may be spent);
- iii. Stage 1.3 – identify limits for gas testing (up to £3,000 may be spent);
- iv. Stage 1.4 – establish supply chain and shipping arrangements for LNG (up to £3,000 may be spent);
- v. Stage 1.5 – design field trial
 - a. Agree trial protocols internally (up to £14,000 may be spent);
 - b. Agree trial protocols externally (up to £11,000 may be spent);
- vi. Other costs (up to £150,000 may be spent)

The Funding Licensee may access £595,000 from the Project Bank Account to undertake the Stage 2 tasks and £15,000 for Stage 3 tasks necessary to take place prior to securing the HSE exemption. This funding is limited to the following:

- i. Stage 2.1 – quantified risk assessment (up to £20,000 may be spent);**
- ii. Stage 2.2 – stakeholder engagement (up to £120,000 may be spent);**
- iii. Stage 2.3 – On-site appliance testing**
 - a. vehicles and kit for testing (up to £30,000 may be spent);**
 - b. conducting testing of all appliances (up to £105,000 may be spent);**
 - c. purchase of gas for testing (up to £20,000 may be spent);**
- iv. Stage 2.4 – procurement and installation of replacement appliances (up to £300,000 may be spent);**
- vi. Stage 3.1 – construction of infrastructure;**
 - a. gas chromatograph site-specific ancillary work (up to £15,000 may be spent)**

The Funding Licensee may not access any other funds from the Project Bank Account for any other activities, including Stage 2 and 3 activities, until the HSE exemption and any additional HSE requirements have been agreed. **If the exemption from the HSE is not secured because it does not consider the approach or sample to be robust, the Authority may re-examine the appropriateness of the use of the funding released for stage two of the project and if deemed inappropriate, make use of the Funding Return Mechanism.**

The Funding Licensee will minimise the total cost incurred against each of these categories. The Authority may audit these costs ex post to ensure that they have been incurred efficiently and only for the purpose of securing agreement for an exemption from the HSE.'

Appendix 2: Updated SDRC submission dates

| Successful Delivery Reward criterion | Evidence |
|---|--|
| <p>Establish supply chain and shipping arrangements for LNG by <u>29 September 2014</u>23 May 2014:</p> <ul style="list-style-type: none"> Investigate possible sources of gas for the trial Review gas prices and logistic costs Confirm and secure gas sources for trial Establish arrangements for gas shipper and nominations into the network Agree supply contract for Trial | <ul style="list-style-type: none"> Value for money commercial contracts in place with Shipper and LNG Producers |
| <p>Carry out a quantified risk assessment by <u>26 June 2015</u>March 2015:</p> <ul style="list-style-type: none"> Identify and understand the risks associated with high Wobbe LNG Create inventory of potential hazards, their likelihood, and consequences assessed by comparison against defined criteria Show that risks are identified and controlled to an acceptable level Build upon existing Risk Assessment associated with existing procedures Project team risk assessment meeting to be held with to discuss and highlight the potential issues and develop a robust view on the potential impact of higher Wobbe Number gases | <ul style="list-style-type: none"> Quantified Risk Assessment published on SGN website Level of risk successfully defined in absolute terms |
| <p>Agreement of Trials with Ofgem, HSE and DECC by <u>18 July 2014</u>:</p> <ul style="list-style-type: none"> Successfully engage with Ofgem, HSE, DECC to agree Project proposals Receive sign on / authorisation to proceed | <ul style="list-style-type: none"> Minutes of meetings documented in Project file Email correspondence documented in Project file Written confirmation of sign on/authorisation to proceed in Project file |
| <p>Testing of all affected appliances by <u>12 June 2015</u>20 February 2015:</p> <ul style="list-style-type: none"> Successfully visit and test all 1104 gas properties and appliances in Oban No entries to be rescheduled and revisited Continued no entry to a property to be investigated and pursued All appliances to be tested and or made safe prior to the start of the trial | <ul style="list-style-type: none"> Appliance test records maintained in Project file |
| <p>Procurement and installation of replacement appliances by <u>24 July 2015</u>:</p> <ul style="list-style-type: none"> Establish number / range / type of appliances to be procured at best value for money Tender installation work to local businesses Review tender returns Evaluate tenders Award tender to best candidate | <ul style="list-style-type: none"> Procurement records for appliance purchase Tender evaluation documentation Appliance installation records from contractor All appliances successfully installed by 24 July 2015 |

| | |
|---|---|
| <p>Construction of required infrastructure by 30 April 2015 <u>21 December 2014</u>:</p> <ul style="list-style-type: none"> • Purchase of necessary equipment • Installation of equipment | <ul style="list-style-type: none"> • Equipment purchase orders • Installation records • Photographic evidence in Project file • Infrastructure successfully installed by 21 December 2014 |
| <p>Field trial successfully completed by <u>14 June 2016</u> 8 February 2016:</p> | <ul style="list-style-type: none"> • Records of monitoring of impacts during trials of different gas types |
| <p>Knowledge dissemination tasks successfully completed by <u>5 August 2016</u> 27 February 2016:</p> <ul style="list-style-type: none"> • Capture network management understanding in terms of pressure, flow and demand profiles • Compile comprehensive report assessing the technical and commercial viability, detailing potential cost benefit • Share knowledge with relevant stakeholder as per dissemination plan | <ul style="list-style-type: none"> • Reports published on Ofgem portal • Presentations to stakeholders • Project video uploaded to You tube site |