

Rupika Madhura  
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Ofgem  
9 Millbank  
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7 July 2016

Dear Rupika,

Re: Consultation on minded-to position on the review of gas transporter agency (Xoserve) costs in RIIO GT1 and T1

Thank you for the opportunity to respond to your consultation on the future funding levels and method for Gas Transport (GT) costs associated with the running of Xoserve in their capacity as the Central Data Services Provider (CDSP). Northern Gas Networks (NGN) has been actively involved in the programme to date to make changes to the funding and governance of Xoserve and continues to engage with this as a high priority.

There are two main elements to this consultation – the overall level of funding for efficient operation of CDS services which remain the overall responsibility of Transporters, and the method by which those costs are incurred in the context of the price control.

#### Overall Allowances

NGN anticipated that the overall costs that would be attributable to Transporters fall in line with a corresponding increase in direct shipper funding of services. There has been considerable work undertaken by the Charging Allocation workgroup, led by KPMG, to assess all services provided and agree across the industry where the funding responsibility would best lie. This work produced an initial high level view that was submitted alongside the Cost Assessment Tables in January 2016, but it is important to consider both the context and detail within this.

The cost allocation work was carried out through a number of detailed working group sessions and focussed on the prevailing, pre UK Link Programme/Project Nexus costs and spread of these across various parties. The work to full determine the precise costs and allocations in ongoing and we believe it is important that the final adjustments to the GT price control is flexible enough to take account of material changes from the initial position taken by the group. This work is ongoing and is expected to deliver a more robust output as part of the overall UNC0565 and Data Service Contract (DSC) solution.

We have noted that Ofgem has considered not only the CAT submitted in January in determining an initial view on overall allowances, but also the Regulatory Reporting Pack (RRP) that was submitted some 12 months ago for the financial year 2014/15. It should be noted that RRP does not include all business costs incurred by Xoserve and the GTs, and therefore these items must be taken into consideration when comparing the two sets of data. Xoserve RRP does not costs associated with projects of less than £0.5m that are undertaken. These projects largely make up delivery of ongoing UNC change together with smaller business improvements that would be considered to be an ongoing element of running Xoserve as a whole. The current Ofgem position does not include these costs or an appropriate allocation to all funding parties.

There are also further changes to both the phasing and actual costs that have taken place between the submission of the RRP and the CAT, which was approved by the Board as the latest business position. Xoserve have carried out an analysis of these costs (appendix 1) and we believe that full consideration of these movements and additional costs need to be included in the overall allowances to be able to ensure that Xoserve can continue to operate with appropriate funding into the future. Without due consideration of both the projects and phasing/changes to other programmes the GT funding element may be insufficient to meet the basic allocation of costs through the charging allocation methodology.

Furthermore, the use of broad percentages applied against total costs of running Xoserve as used by Ofgem for determining the proposed allowances does not take account of the nuances of a bottom up approach used in the charging methodology paper. We are concerned that this may lead to price control caps which are not flexible enough to take account of more detailed cost allocation and may lead to distortion between the services agreed to be funded by parties and the amount they are allowed to pay for them.

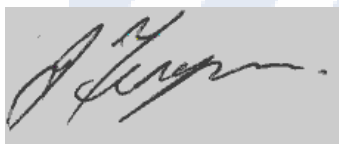
#### Method of funding

We have noted previously that Ofgem had taken a view that variability of costs to GTs would be treated as pass through rather than a fixed allowance. This would enable GTs to have a better balance of costs versus control as both the charging methodology and Board of Directors moves to a more collaborative model of governance. The minded-to position to retain a lower price controlled allowance, while removing some elements of control of costs will place the GTs in a different position from the other funders of Xoserve services. By placing a fixed allowance onto the GTs it is likely to remove flexibility for ensuring that the charging methodology can evolve to remain cost reflective of the services incurred by each party. It is also likely to remove the ability of the GTs to fund general improvements that were not foreseen at the time that the price control was set.

While we understand the view that the industry has not shown sufficient co-operation and flexibility in recent project to remove the element of Authority control, we believe that it is important that the model used does not lead to friction between funding parties in agreeing both the overall costs of individual projects and services, but also the sharing arrangements between the parties. We would welcome an ability to further flex the allowance baseline should efficiently incurred additional costs be identified over the remainder of the price control, in particular costs associated with industry led change which require an element of GT funding which was unforeseen at the time of setting the allowances.

I hope you find these comments useful and please contact me should you require further information.

Yours sincerely,



Joanna Ferguson  
Regulation & Industry Codes Manager

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Appendix 1

**CDSP Core Services Variance Analysis 2014/15 RRP to January 2016 CAT submission  
Cumulative trace for the period 2017/18 to 2020/21  
£m 2014/15 prices**

<b>2014/15 RRP submitted to Ofgem for 2017/18 to 2020/21</b>		<b>212.2</b>
Adjustment for Projects <£0.5m not required to be reported		6.7
<b>2014/15 RRP complete "CDSP" cost base</b>		<b>219.0</b>
<b>Running the Business variances</b>		
<u>Resource movements</u>		
Deferral of UK Link Programme to Oct 16	1.5	
FGO Director fees & Searches	1.8	
Workload FTE changes	0.2	
User Pays resources reallocated to Core Services	1.0	
Rates changes (Salaries, Employers NI, DB scheme)	3.0	7.6
<u>Bought in Services</u>		
Property		1.2
<u>IS Core Services</u>		
Deferral of UK Link Programme to Oct 16	1.7	
Revision of other IS services	-0.9	0.8
<b>Total RTB variance</b>		<b>9.5</b>
<b>Investment Variances</b>		
<u>Transmission Funded</u>		
EU / GB change	2.8	
Gemini Rewrite	7.6	10.3
<u>Other change</u>		
UK Link related	0.7	
Non UK Link related	1.4	2.1
<b>Total Investment variance</b>		<b>12.4</b>
<b>January 2016 CAT submission</b>		<b>240.9</b>
<b>Increase in CDSP Core Services cost base</b>		<b>28.6</b>