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Your Reference: UNC Modification Proposal 0550

UNC Modification Proposal 0550 - Project Nexus: Incentivising Central Project Delivery

Dear Bob,

Thank you for your invitation seeking representations with respect to the above Modification Proposal which National Grid Gas Distribution (NGD) does not support.

Do you support or oppose implementation?

Oppose

Reason for support/opposition: Please summarise (in one paragraph) the key reason(s)?

NGD believes that the proposed 'incentive' contained within the Modification constitutes a financial penalty/sanction. Our view is that this would also create a highly undesirable precedent in UNC which could encourage inappropriate behaviours from Code parties concerning future systems and process implementation programmes.

Implementation

This Modification Proposal could be implemented with immediate effect.

Impacts and Costs

Implementation of this Modification would have the effect of placing a very substantial and unfunded financial penalty (up to £10m) on Gas Transporters. This is over and above the costs Transporters would inevitably incur as a consequence of any future delay in implementation of Project Nexus.

Legal Text

As providers of the legal text and associated commentary, NGD is satisfied that this meets the requirements of the Modification.

Are there any errors or omissions in this Modification that you think should be taken into account?

We have not identified any errors or omissions within this Modification Proposal.

Please provide below any additional analysis or information to support your representation

We do not believe any additional analysis or information is necessary.

Is there anything further you wish to be taken into account?

NGD has raised and led development of the majority of UNC Modifications pertaining to Project Nexus. We are disappointed that there has been a series of delays to implementation of the systems solution underpinning implementation of the 'core' Nexus Modifications (0432, 0434 and 0440). However, we are determined to take whatever measures we can to ensure the 1st October 2016 implementation date is met, for example by raising any UNC Modification Proposals which may be necessary to facilitate this. We have also challenged our Agency, Xoserve at a senior level within our organisation to encourage prompt delivery of the project milestones and to emphasise the priority which should be placed on timely implementation of the UK-Link replacement programme.

Notwithstanding the above, we have considerable reservations with regard to the adverse effects on the UNC regime that would materialise as a consequence of implementation of this Modification Proposal. We have identified these below:

Incentive

NGD believes that this Modification does not in any respect constitute an incentive to deliver the Project Nexus Modifications. All UNC parties have a 'best endeavours' obligation under UNC. This is a high level of legal 'test' and consequently NGD has placed a very high priority on delivery of the systems solution, using all means at its disposal to ensure its Agency, Xoserve, meets the Project Nexus implementation timetable.

Regular checkpoint meetings between Transporters and Xoserve at board level have occurred, including the involvement of Xoserve's systems development service provider. Significant challenges have been brought to bear at a Director level within our organisation to ensure Xoserve employs all measures at its disposal to expedite timely implementation. This has included recruitment of additional labour resources and significant re-prioritisation of activities. In this respect we believe Xoserve is doing everything it possibly can to ensure that the 1st October 2016 date is met.

Consequently there is nothing in this Modification Proposal, if implemented which would 'incentivise' Transporters to take any further steps to facilitate Nexus implementation than those already being taken. From this our conclusion is that it constitutes a clear and unambiguous penalty payment to be made by the Transporters in the event the Project Nexus Implementation Date is not achieved.

Precedent

We believe that this Modification if implemented would create a significant and highly undesirable precedent within UNC. There is not, and never has been an arrangement of this nature within the UNC or its predecessor, the Transco Network Code. We would comment that the examples cited in Section 6 'Impacts' of the Draft Modification Report bear no resemblance to the solution proposed in this Modification. Typically, an incentive scheme under the UNC should be 'balanced' with parties able in some circumstances to outperform on a standard and therefore be proportionately rewarded for

good performance. Such an arrangement is also an underpinning tenet of the RIIO regulatory framework.

The inclusion of a penalty based principle such as this could have far reaching ramifications for future change under the UNC. We are fearful that as a consequence, whenever any change initiative or aspiration is identified, whether this is major or minor, parties will be wary of progressing this being mindful that any other party might seek to 'incentivise' delivery of a supporting process or systems solution through a financial penalty. Our view is that the imposition of a finance based penalty framework such as that contained within this Modification Proposal could stifle change and innovation through parties not wishing to subject themselves to unwarranted financial risk. Furthermore going forward a 'risk premium' would undoubtedly need to be factored into any prices or cost recovery in respect of 'incentivised change'.

Our opinion is that the notion of a collaborative industry approach to change is seriously compromised and therefore the well-established nature of UNC development, being that based on co-operation and agreement is changed radically and certainly over time to the detriment of gas customers.

Identification/attribution of fault

The Modification provides for the Authority to determine whether it is the Transporter's fault for the UK-Link replacement system not being delivered on time. We are not aware of such a process previously existing within the UNC or Transco Network Code. This could establish an industry assumption/expectation that Ofgem would be able to determine a range of UNC (and other Code) matters over and above those decisions Ofgem normally makes in accordance with the UNC modification process. This expectation we believe would create considerable uncertainty and risk exposure for Ofgem should they need to make any such determinations.

There is no methodology or requirement to set guidelines within the Modification on the criteria by which Ofgem would make a determination of fault. There is also no reference to or requirement for any analysis which might be required to support an informed determination of accountability. This is clearly inconsistent with the UNC change process where Ofgem is required to make an implementation decision based on fully available and transparent industry information and analysis as required. Their direction is also required to be based on a number of clear and unambiguous 'relevant objectives' which are set out within the GT Licence. We believe these well-established safeguards are absolutely essential for the protection of all parties including Ofgem.

Determination of level of incentive

The Modification states that "Due to the nature of an incentive payment it is not required to be an accurate or genuine pre-estimate of Gas Shipper loss. It is provided to incentivise delivery and is not required to compensate Gas Shippers for loss however in this case the proposer feels that this value is relevant and reasonable and is believed to be roughly 10% of the costs of the initial delivery programme previously estimated at £70m whilst no other industry information has been forthcoming". We would comment that no analysis has been undertaken to assess whether the proposed incentive is "relevant and reasonable". It is an arbitrary value determined by the Proposer and the absence of any underpinning rationale for this is concerning given the large monetary value of the proposed 'incentive'.

We trust that this information will assist in the compilation of the Final Modification Report. Please contact me on 01926 653541 (chris.warner@nationalgrid.com) should you require any further information.

Yours sincerely,

Chris Warner
Stakeholder Implementation Manager, Distribution