

Stakeholder consultation - Sale of a majority stake in National Grid's Gas Distribution Network business

On 10th November, National Grid announced a process to sell a majority stake in its UK Gas Distribution Business. Currently, we own 4 out of 8 Gas Distribution networks in the UK and deliver gas to around 10.9million customers.

Since November we have been planning what needs to be done in preparation for a sales process. We have started discussions with Ofgem as they have a role to play in consenting to the licence changes and transfer of assets to a new buyer.

As an important stakeholder in the industry, we would like to get your views. Specifically on the services that National Grid provides and the industry depends on and how these will continue to be provided.

Some key facts on the Gas Distribution business are set out below.

- Distribution networks transport gas from the high pressure transmission network and deliver it to homes and businesses
- There are eight regional gas distribution networks in Great Britain, four of which are owned and operated by National Grid
- Our four UK networks comprise 82,000 miles (131,000km) of pipeline and serve 10.9 million consumers
- National Grid does not own or sell gas directly to consumers – that is the role of the energy suppliers
- Our gas distribution networks operate at 99.999% reliability



Having your say

Since the announcement we have been planning what needs to be done to make a sale possible. We are now in a position to explain our proposals to you so that you can understand the implications for the services that you receive.

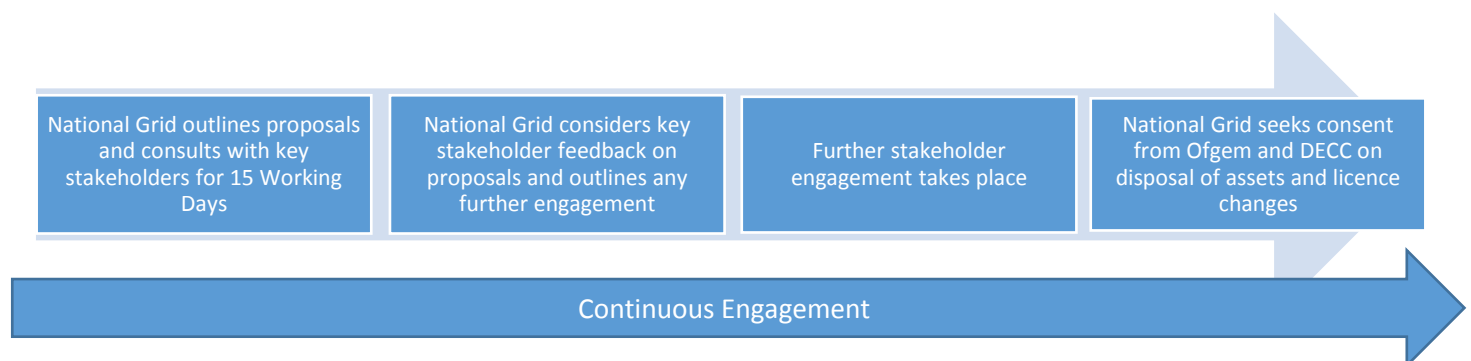
The industry has seen a number of changes in ownership over recent years and our belief is that whilst the ownership of National Grid's gas distribution networks will change as a result of the sale, stakeholders who are recipients of services are expected to see no change.

We think it is helpful however to explain this to you in the context of some of the services that both our Distribution and Transmission regulated businesses participate. In this document we explain our proposal and how key services delivered to the industry will continue to be provided. The specific areas are:

- Joint Office of Gas Transporters (page 4)
- Backstop meter provider of last resort (page 6)
- 0800 Gas Emergency number (page 8)
- Xoserve (page 9)

Importantly, we also want to assure you of the commitment of the Gas Distribution business to meeting its RIIO outputs, which will remain unchanged by the Gas Distribution Sale, as will its commitment to customers and stakeholders.

During this consultation, we feel it is important for our stakeholders to have a say on the proposals outlined in this document. We are asking for initial views or comments to be fed back to National Grid by **8th March 2016** and we will follow up with stakeholders after this period to address specific matters. Where options are presented please indicate your preferred options, or no preference, as the case may be, with an explanation of your reasons. This will help us understand the views and any concerns of our stakeholders and will be used to inform further activity and /or recommendations below.

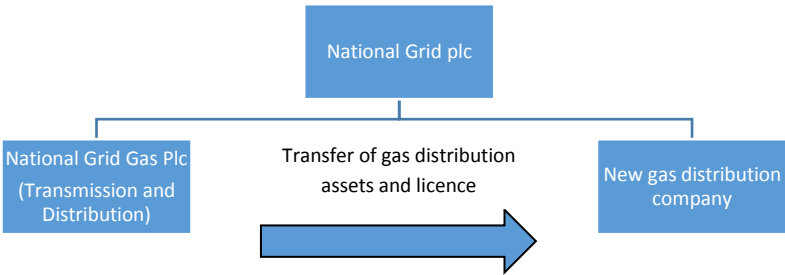


We have set-up a dedicated e-mail address which you can now use to register any questions or viewpoints you would like to raise. You can do this by sending an e-mail to box.GDXHaveYourSay@NationalGrid.com. Alternatively, if you would like to someone at National Grid to contact you back, please in the first instance contact Kim Lynch (Kim.Lynch@NationalGrid.com) outlining your issue.

Gas Distribution Sale

National Grid owns the high pressure gas transmission network and four gas distribution networks in Great Britain within one legal entity, National Grid Gas plc. Separate gas transporter licences are held in respect of the Transmission and Distribution businesses, that is to say there is one Distribution licence and one Transmission licence.

In order to facilitate the proposed sale it will be necessary therefore to transfer the Distribution assets and Distribution licence out of National Grid Gas plc into a new company, within the National Grid group. This process is shown below (note there are more companies in the group than shown).



Following the proposed transfer of the Gas Distribution licence and assets, a majority stake in the new distribution company will then be sold to a third party.

Ofgem and the Secretary of State for Energy and Climate Change are required to give consent to the transfer of the gas distribution assets and licence. The Health and Safety Executive will also need to give approval to the new safety case which will be prepared for the new gas distribution company.

The remainder of this document sets out four key areas of service provision which we think it would be helpful to explain to our stakeholders. We have included questions after each section that we would appreciate our stakeholder’s responses to, so that we can address any points raised.

1. Joint Office of Gas Transporters

Background

The Joint Office of Gas Transporters provides governance around the processes for modifying the Uniform Network Code (UNC). This is done through the website of the Joint Office of Gas Transporters and in meetings, which the Joint Office administers. The requirement to have joint governance arrangements is set out in Standard Special Condition A12 of the transmission and distribution licences. The Joint Office of Gas Transporters is staffed by representatives from the transmission and distribution network operators who are relevant gas transporters. Relevant gas transporters are those who hold a gas transmission or distribution licence in which Standard Special Condition A12 is effective; National Grid Gas Transmission and Distribution, and the four other Gas Distribution Networks (GDNs).

All relevant gas transporters are required to be a party to the Joint Governance Arrangements Agreement (JGAA).

Current State

Currently both National Grid Gas Transmission and National Grid Gas Distribution are relevant gas transporters and are parties to the JGAA (as are the other Gas Distribution Networks); as such, both businesses have representatives on the Joint Governance Arrangements Committee (JGAC).

Each party to the JGAA has an obligation to bear the remuneration costs for its representative(s) and be responsible for funding a proportion of the expenditure of the Joint Office in line with the following equation:

$$\frac{\text{Aggregate Approved Expenditure} \times \text{Number of Networks Owned}}{\text{nine}}$$

National Grid Gas Distribution currently bears the cost of the four networks within its ownership and funds its own JGAC representative.

Effect of the transfer

At the point of transfer of the gas distribution assets and licence from National Grid Gas plc to the new gas distribution company, the following will take effect :

- National Grid Gas plc will cease to be a relevant gas transporter in respect of its gas distribution business only and therefore will cease to be a party to the JGAA in that capacity. This will mean the removal of National Grid Gas plc's Distribution representative on the JGAC and removal of the obligation to provide associated funding;
- At the same time, the new gas distribution company will become a relevant gas transporter and will become a party to the JGAA by signing an Accession Agreement. We expect that the same person will be appointed by the new gas distribution company as its representative on the JGAC and the new gas distribution company will be obliged to provide the same level of funding as National Grid Gas plc currently has in respect of the Gas Distribution business.

There is no impact on National Grid Gas plc's membership or obligations in respect of its transmission business.

Gas Distribution sale will cause no change to the services that the Joint Office provides.

Position at Sale Completion

At the point at which the sale of a majority stake in the new Gas distribution company completes the position will remain largely unchanged from that at the new gas distribution company creation, the only major difference is that the National Grid group will be a minority shareholder in the new gas distribution company.

Summary of Gas Distribution Sale impact on Joint Office

It is anticipated there will be no change to the services provided by the Joint Office as a result of the Gas Distribution Sale.

The licence condition concerning Joint Office in National Grid Gas plc's licence is not expected to change and subject to consultation will transfer with National Grid Gas plc's licence to the new distribution company.

The existing commercial arrangements and funding obligations will apply to the new owner of the gas distribution business and it is expected there will be no change of representation on the JGAC.

Resourcing of the Joint Office is subject to the wider consideration about the transfer of National Grid staff into the new gas distribution company; however the resourcing of the Joint Office is expected to remain largely unchanged.

Question for stakeholders: Do you agree with our proposals for the Joint Office?

2. Backstop meter provider of last resort obligation (BMPoLR)

Background

National Grid Gas plc provides certain regulated domestic metering services to distribution gas transporters pursuant to obligations in its Gas Distribution licence. The service is provided to suppliers, by National Grid Metering Limited, a Meter Asset Manager (MAM).

The meter provider of last resort obligation (MPoLR)

Gas Distribution Licence Obligations applicable to all Distribution networks

Each of the licences in respect of the eight gas distribution networks contain an obligation to provide a meter, within the geographical boundary of that network, to domestic premises, where requested by a gas supplier. This provision must be through a MAM and on published terms. Those terms and the provision of the service must be offered without undue preference or undue discrimination. Standard Special Conditions D17, D18 and D19 of the gas distribution licence set out these obligations. The obligations refer only to domestic premises and only to the older (“traditional”) meter type. The obligations do not apply to smart meters.

The market for traditional meters

The demand for traditional meters is predicted to decline over the next few years as an increasing number of smart meters are installed in domestic premises. There is competition in the provision of traditional meters.

To manage the transition to smart meters and an orderly run down of the market for traditional meters, the above licence obligations set out that a supplier will be able to request the provision to a customer of a traditional meter through the expected period of transition. We do not anticipate any of the above will be impacted by the Gas Distribution Sale. These licence conditions should continue to exist in the licences of all gas distribution networks, including, for avoidance of doubt, in the licence to be held by the new gas distribution company. Customers and stakeholders who currently enjoy meters provided under these arrangements should not experience any change to service provision.

BMPoLR

The licence held by National Grid Gas plc in respect of its Gas Distribution business has an additional obligation, not contained in the licences of the other GDNs. This obligation requires that where an GDN receives a request from a supplier to provide a meter under Standard Special Condition D17 (as above), within its geographical area, it can require National Grid Gas plc to fulfil that request on its behalf by requiring a MAM to provide the service. These obligations are set out in Chapter 5, Special Conditions 5A and 5B of National Grid Gas Distribution’s Licence.

This service is currently provided by National Grid Metering Limited on behalf of National Grid Gas plc, with National Grid Metering Limited managing the gas supplier relationship.

Gas Distribution Sale implications

The question for the Gas Distribution Sale is where the BMPoLR obligation set out in Special Conditions 5A and 5B should reside. Whatever solution is reached, we expect that customers of that service will see no change to service provision. Subject to regulatory consent, the following solutions are possible.

Option One

When the assets and licence of National Grid Gas Distribution are transferred to the new gas distribution company, the licence could be modified to remove the BMPoLR obligation from the new gas distribution company's licence. In this scenario, the only other possible place for this obligation to reside would be in the Gas Transmission licence held by National Grid Gas plc in respect of its high pressure transmission pipeline business. The consequences of this option would be no material change to the existing contracts which National Grid Gas plc has with suppliers. There would be no changes to how the service is delivered, as National Grid Metering Limited is not part of the Gas Distribution Sale.

Option two

Under this option, when the assets and licence of National Grid Gas Distribution are transferred to the new gas distribution company, this backstop obligation would be transferred in the existing Gas Distribution licence to the new gas distribution company which would be responsible for the BMPoLR obligation. The practical consequences of this option are that the contracting framework would need to be reviewed so that the new gas distribution company could discharge the BMPoLR licence obligation through a MAM.

Option two would result in the new distribution company's licence having BMPoLR (a backstop licence obligation that is designed to protect consumers on all of the distribution networks) in its licence only. In addition, there would need to be changes to the metering contracts to enable the new gas distribution company to discharge this obligation.

Summary

As Option One presents no material change to commercial arrangements for the industry this is the most straightforward solution. Additionally it ensures that the licences of all Distribution transporters have the same obligations in respect of metering. Clarity of contracting parties and hence accountability is expected to remain as they are today.

Question for stakeholders: Which would be your preferred option and why?

3. 0800 Emergency Number Provision

Background

The requirement for the provision of a continuously manned telephone service for reporting gas escapes is set out in Regulation 7 of the Gas Safety (Management) Regulations 1996 (GS(M)R). The duty holder in GS(M)R is named as British Gas plc. Today, National Grid Gas plc, as successor in title to British Gas plc, is the duty holder. The 0800 number activity, which consists of a call receipt and management service for the reporting of gas emergencies, is carried out by National Grid Gas Distribution on behalf of the other GDNs, Transmission, and Independent Gas Transporters.

The duty in GS(M)R

The effect of separating National Grid Gas Distribution from the legal entity National Grid Gas plc would leave the duty holder and the existing call management provider in different legal entities. The new gas distribution company appears to be the appropriate entity to continue to provide this important service and the assets, people, systems and contracts will need to transfer to the new gas distribution company.

We are discussing with the Health and Safety Executive the most appropriate way to ensure that the obligation continues to align with the delivery of the service. In any event, the impact of the Gas Distribution Sale will leave the service unchanged and with clear accountability.

The solutions that we are discussing with the Health and Safety Executive include creating the flexibility for future changes in the duty holder, so that the current limitation in GS(M)R is removed. This would facilitate the duty holder being either a category of persons or perhaps more widely, any suitable person possessing appropriate skills, resources and expertise, that might wish to be a provider of this service.

Summary

In summary, our proposal is that the existing activity stays with the Gas Distribution business (and therefore transfers from National Grid Gas plc to the new gas distribution company), which presents no change to the way that the service is provided today and therefore avoids any risk that might arise through changing existing arrangements.

National Grid will clarify these changes within the Safety Case document for both National Grid Transmission and the new gas distribution company.

There will be clear accountability for delivery of the service at all times.

Question for stakeholders: Do you believe the duty to provide the 0800 number should remain with the gas distribution business as a result of the Gas Distribution Sale? If not, why?

4. Xoserve

Background

Standard Special Condition A15 of both the gas Transmission and Distribution licences outline the requirement for all relevant gas transporters to enter into an agency services agreement for the common provision of certain services and systems. The agency referred to by the licences is Xoserve Limited and the agency services agreement (ASA) is a commercial agreement which all relevant gas transporters are party to.

Licence conditions

There is no requirement to make changes to the gas Transmission or Distribution licence conditions relating to Xoserve as they are written to accommodate a change in network ownership. Standard Special Condition A15, which is in each of the gas distribution and transmission licences, will be in the licence transferred to the new gas distribution company.

Funding, Governance and Ownership (FGO) consultation

The industry is undertaking a review of the funding and governance of Xoserve and the agency services that are provided to the industry. This has been the subject of extensive consultation which is set out on Ofgem's website. We believe the Gas Distribution Sale does not result in any changes to this process.

Ownership share of Xoserve

The share capital of Xoserve is split between the gas transporters of the eight gas distribution network and gas transmission (a total of nine separate shareholdings). When the assets and licence of National Grid Gas's distribution business transfer to the new distribution company, National Grid Gas plc's shareholding in respect of its four gas distribution networks automatically converts to deferred shares (i.e. with no ownership rights). The new distribution company will be issued new shares (being the same number of shares previously held by National Grid Gas plc in respect of its gas distribution business) subject to it acceding to the required industry commercial agreements being (i) the shareholders' agreement; (ii) a consortium Deed of Adherence (related to tax); and (iii) the ASA.

Summary

Save for the ownership change set out above it is expected there will be no impact to Xoserve or the services it provides as a result of the Gas Distribution Sale.

The new gas distribution company will become the owner of the same number of shares representing the 4 gas distribution networks as currently owned by National Grid Gas plc.

Question for stakeholders: Do you have any concerns regarding the services Xoserve provide as a result of the proposed Gas Distribution sale?

5. Other matters necessary for Gas Distribution Sale

1. The new distribution company will accede to the UNC and will become a party in the same way that National Grid Gas plc is currently a party in respect of its gas distribution business. The UNC is currently being reviewed to consider any changes required. These are thought to be referencing changes only but when the review concludes, any modifications required will be brought forward in the usual way, in the near future.
2. A review is also being undertaken to assess any required changes to the existing consents and derogations granted to National Grid Gas plc under the gas distribution licence. Any required changes will be progressed with Ofgem in the usual way.

Question for stakeholders: Is there anything else you believe should be taken into account as part of the Gas Distribution sale? If so, what do you believe this to be?

Consultation steps

We hope that the above is helpful in setting out the limited changes to the relevant regulatory frameworks that are necessary in order for the Gas Distribution Sale to proceed. We believe that our stakeholders will not see any changes to the services provided as a result of a change in ownership of the gas distribution business.

We are asking for any initial views from stakeholders by **8th March 2016**. This is important to us as this will enable us to understand and plan how we can best respond to any concerns of our stakeholders on the Gas Distribution sale moving forward. We look forward to discussing this with you.

All feedback should be sent to box.GDXHaveYourSay@NationalGrid.com, or alternatively as aforesaid, if you would like someone at National Grid to contact you, please contact, in the first instance, Kim Lynch (Kim.Lynch@NationalGrid.com)