

May 1999

## **Grant of a Shipper Licence to BG Gas Services Ltd**

### **Decision Document**

# GRANT OF A SHIPPER LICENCE TO BG GAS SERVICES LTD

## DECISION DOCUMENT

### 1. Introduction

On 19 March 1999 Ofgas consulted on an application by BG Gas Services Ltd (GSL) for the grant of a gas shipper licence under Section 7A(2) of the Gas Act 1986.<sup>1</sup> Ofgas indicated that it was minded to grant a licence, and was minded to include in that licence certain special conditions. This document summarises the responses to that consultation and explains Ofgas's decision.

### 2. Ofgas's Decision

Ofgas decided to grant a licence subject to the special conditions set out in the consultation document. A copy of the licence is included as Appendix 1 to this document. Ofgas has also written to GSL and to BG plc explaining how it intends to enforce the licence conditions. A copy of that letter is included as Appendix 2 to this document.

### 3. Background

GSL is a subsidiary of BG Exploration and Production Ltd (E&P), which is itself a subsidiary of BG plc (BG). BG owns and operates the main gas transportation system in Great Britain. In that capacity, BG is licenced as a public gas transporter (PGT) and trades as Transco. GSL applied to Ofgas for the grant of a gas shipper licence on 15 March 1999.

---

<sup>1</sup> *The Grant of a Gas Shipper's Licence to BG Gas Services Limited, A Consultation Paper Ofgas, March 1999.*

The Gas Act 1986 (the “Gas Act”) prohibits the holder of a PGT licence from also holding a shipper’s licence, and similarly prohibits the holder of a shipper’s licence from holding a PGT licence. There is no restriction on a subsidiary of a PGT from holding a shipper’s licence or on a subsidiary of a shipper from holding a PGT licence. Currently 6 PGT licences are held by subsidiaries of groups that also hold shipper licences. However, in each of these existing cases the PGT business involved is relatively small. In contrast, Transco enjoys a unique position as owner and operator of the main gas transportation system in Great Britain.

Given Transco’s unique position, Ofgas had a number of concerns regarding the grant of a shipper licence to a subsidiary of BG. These were:

- the potential for cross-subsidies between BG and GSL;
- the potential for Transco to offer beneficial commercial terms to GSL;
- the danger of inappropriate information flows between Transco and GSL; and
- the danger that staff transfers between Transco and GSL might allow the transfer of commercially sensitive information.

These concerns were explained in more detail in Section 5 of the consultation document.

BG’s PGT licence contains a number of standard and special conditions which might be expected to prevent these problems arising – or provide the Director General of Gas Supply (DGGS) with powers to remedy any problems that did arise. However, Ofgas was concerned that obligations also needed to be imposed on GSL itself to prevent these problems arising, and that the DGGS should be able to take enforcement action against GSL directly if a breach of these obligations arose. Ofgas was also concerned that it should be able to detect any cross-subsidisation of GSL by BG. Ofgas therefore proposed to include the following special conditions in GSL’s shipper licence, if granted:

- a requirement that GSL's shipping business produce separate accounts so that Ofgas could more easily identify any cross-subsidy;
- a requirement on GSL to conduct its business in a manner which would prevent it gaining any unfair commercial advantage from its links with Transco;
- a prohibition on GSL seeking or receiving inappropriate information from Transco;
- a restriction on staff movements between Transco and GSL; and
- a requirement to appoint a compliance officer (who could be the existing compliance officer employed by BG) to ensure compliance with the various obligations placed on GSL.

These special conditions were explained in more detail in Section 6 of the consultation document.

#### **4. Responses to the Consultation**

Ofgas received responses from 10 companies and organisations. Nine of the respondents are listed in Appendix 3; the tenth response was confidential. A summary of the points raised in the nine public responses, and Ofgas's reaction to these points, is set out in Appendix 4.

##### ***Consultation Issues***

Ofgas invited comments on whether:

- a) GSL should be granted a shipper licence;
- b) Ofgas had correctly identified the potentially anti-competitive arrangements;
- c) Ofgas was correct in its view that no additional conditions were required in BG's PGT licence; and

- d) the special conditions that Ofgas intended to include in GSL's gas shipper's licence were necessary and sufficient to address these potentially anti-competitive arrangements.

The main arguments made on each point, and Ofgas's conclusions on each issue, are summarised below.

**a) *Should GSL be granted a gas shipper's licence?***

The majority of responses supported Ofgas's intention to grant a licence. Three opposed the granting of a licence, and between them advanced three main arguments:

- although the Gas Act does not proscribe the granting of a licence to the subsidiary of a PGT licence holder, this does not provide automatic grounds for granting a shipper's licence;
- although some shipper licences are already held by companies within groups that also hold PGT licences, these PGT licensees are much smaller than Transco and do not provide a precedent for granting a shipper's licence to a subsidiary of BG; and
- if a licence were granted, there would be an inherent conflict of interest within the BG group between Transco's obligations as a PGT and GSL's commercial interests as a gas shipper. Specifically, Transco will always have an incentive to favour GSL since both are part of the BG group and share a common commercial interest. This conflict cannot be overcome by licence conditions.

On the first argument, Ofgas could not refuse to grant a licence simply because the grant of licences is discretionary. An application should be refused only on a rational basis in accordance with the DGGS's relevant duties, such as his duty to secure effective competition in the carrying on of shipping and supply. Ofgas would also need to consider whether it was possible to overcome the difficulty arising from the grant of a licence by imposing relevant licence conditions. In this case Ofgas has concluded that the grant of a licence is consistent with the DGGS's duty in relation to competition in gas shipping, providing the special conditions described in the consultation documents are included in the licence.

On the second argument, Ofgas agrees that this application is different from the situation where a shipper – perhaps with a relatively small share of the shipping market – applies for a new PGT licence. Transco can be assumed to be dominant in the provision of transportation services and that is why special conditions have been included in GSL’s licence.

The third argument raises the question of whether it is appropriate for BG, as operator of the main gas transportation system in Great Britain, also to participate in activities such as the production, shipping or supply of gas. By undertaking any of these activities in a market for gas in Great Britain, BG becomes, directly or indirectly, a user of Transco’s network. For example, as a producer, it delivers gas at the beach for transportation via the Transco network.

Any interaction between BG’s gas-production activities and its Transco network raises the potential for favourable treatment by Transco that could distort competition. Ofgas takes these risks seriously. BG’s PGT licence contains conditions requiring it to conduct its transportation business in the manner best calculated to avoid any unfair commercial advantage to related businesses, which include E&P. BG is also subject to relevant competition law. If Ofgas found evidence that BG was using its position as a PGT to favour its gas production activities Ofgas would take action under its existing powers.

These risks exist at present because of the ownership by BE and E&P; they would not be created by granting a shipper licence to GSL. Ofgas does not consider it appropriate to refuse to grant a licence on these grounds. In Ofgas’ view the grant of a licence with special conditions strengthens overall its power to regulate the BG group. Nor does Ofgas consider it appropriate, in the absence of evidence that E&P currently benefits from anti-competitive behaviour by Transco, to require divestment of all or some of BG’s non-transportation activities as a condition for granting a shipper licence.

Nevertheless, Ofgas recognises that granting a shipper licence to GSL may increase the risk of competition distortions occurring. This is why Ofgas has included special conditions in GSL’s shipper licence and is taking further action to ensure that these conditions are fully observed.

***b) Has Ofgas correctly identified the potential anti-competitive arrangements?***

Respondents suggested a number of anti-competitive effects that Ofgas had not specially identified, including:

- GSL and Transco could collude in the flexibility mechanism or the proposed on-the-day commodity market;
- Transco could distort decisions on the allocation of capacity to favour GSL, or distort decisions on the enhancement of capacity to favour E&P;
- Transco could discriminate in favour of GSL in its decisions on interruptions; and
- problems could arise if GSL and Transco are allowed to share premises or computer networks.

Ofgas agrees that these risks need to be addressed. Ofgas therefore is taking the action described in section (d) below to address the first concern. Ofgas believes that the second and third concerns should be addressed by Special Condition 3 of GSL's licence and by Standard Condition 11 of BG's PGT licence. Ofgas believes that the fourth concern is addressed by Special Condition 3 of GSL's licence and has reminded BG of its responsibilities in the letter reproduced at Appendix 2 to this document.

***c) Was Ofgas correct in its view that no additional conditions were required in BG's PGT licence?***

Some respondents argued that BG's PGT licence should be amended to prevent GSL sharing premises with Transco or receiving cross-subsidies from Transco. Ofgas concluded that Standard Conditions 2 and 11 of BG's PGT licence (as they are amended in their application to Transco) already addresses these issues effectively from the standpoint of Transco, so the PGT licence does not require amendment.

***d) Are the proposed special conditions necessary and sufficient to address these potentially anti-competitive arrangements?***

One respondent argued that the special conditions proposed by Ofgas for GSL were unnecessary. Ofgas disagrees. In particular, Ofgas believes it is necessary for GSL to produce separate accounts for its shipping business so that any cross-subsidy by BG can be identified. It is also necessary to include conditions concerning undue advantage or discrimination in GSL's licence so that (if a breach occurred) enforcement action could be taken against both BG and GSL.

Some of the other respondents suggested three additions to the special conditions proposed by Ofgas:

- the licence should require the separation of Transco and GSL's computer systems and premises;
- BG should be required to establish an audit trail for all transactions in the flexibility market between Transco and GSL; and
- GSL should be required to submit to Ofgas its bid strategy for the flexibility mechanism.

Ofgas agrees that BG should be required to comply with the first two measures but has concluded that they can be achieved using the existing and proposed licence conditions. Ofgas has written to Transco the letter reproduced at Appendix 2. The letter sets out Ofgas's expectation that BG will ensure appropriate separation of computer systems and premises, in order to comply with its licence conditions. Ofgas expects the licence conditions to lead to BG maintaining an accurate audit trail of all transactions between GSL and Transco.

Ofgas also considered whether GSL should be required to submit a flexibility-mechanism bidding strategy. Ofgas has concluded that this is not appropriate, since GSL will not, by itself, be dominant in the flexibility mechanism. GSL will be prohibited by Special Condition 3 of its shipper's licence from obtaining information from Transco in order to exploit this information when trading in the flexibility mechanism (or the proposed on-the-day commodity market). Transco is similarly



restricted from providing such information to GSL. GSL has also agreed to supply Ofgas with details of all trades conducted in the flexibility mechanism to allow an immediate investigation of any allegations that GSL or Transco has contravened this licence condition.

Ofgas believes these actions will address the concerns raised above.

THE LICENCE GRANTED TO BG GAS SERVICES LTD

OFGAS

GAS ACT 1986  
SECTION 7A(2)

GAS SHIPPER LICENCE

GRANTED TO

BG Gas Services Limited

31 March 1999

**Gas Shipper Licence granted under section 7A(2) of the Gas Act 1986 to  
BG Gas Services Limited**

1. The Director General of Gas Supply (“the Director”), in exercise of his power under section 7A(2) of the Gas Act 1986 (c.44) as amended (“the Act”), hereby grants to BG Gas Services Limited (company number 3299002), the registered office of which is situated at 100 Thames Valley Park Drive, Reading RG6 1PT, a Licence authorising the Licensee to arrange with any public gas transporter for gas to be introduced into, conveyed by means of or taken out of a pipeline system operated by that public gas transporter during the period specified in paragraph 2 below, subject to -
  - (i) the Conditions set out in Schedule 1 hereto (“the Special Conditions”);
  - (ii) the Standard Conditions of Gas Shippers’ Licences as from time to time amended in accordance with the terms of the Act which shall be incorporated by reference in this Licence with such amendments as are set out in Schedule 2 hereto (“the Standard Conditions”); and
  - (iii) revocation in accordance with Schedule 3 hereto.
2. This Licence shall take effect on 31 March 1999 and shall continue in force until 22nd August 2011 (being 25 years from the date appointed under section 3 of the Act), and thereafter until determined at or after the expiry of that period by notice in writing served by the Director on the Licensee on a day at least 10 years before the notice is to take effect.
3. Without prejudice to sections 11 and 23(1) of the Interpretation Act 1978 (c.30)-
  - (a) this Licence shall be interpreted and construed in like manner as an Act of Parliament passed after the commencement of the said Act of 1978; and
  - (b) expressions used in this Licence which are also used in Part I of the Act shall, except where the context otherwise requires, have the same meaning as in that Part.
4. The provisions of section 46(1) of the Act (service of notices, etc.) shall have effect as if set out herein and as if for the words “this Part or regulations made under this Part” there were substituted the words “this Licence”.

The Official Seal of the Director  
General of Gas Supply hereunto affixed  
is authenticated by:-

.....  
Authorised in that behalf by the  
Director General of Gas Supply

31 March 1999

**SCHEDULE 1**  
**to the**  
**Gas Shipper Licence granted under section 7A(2) of the Gas Act 1986 to**  
**BG Gas Services Limited**

**SPECIAL CONDITIONS**

**Condition 1: Interpretation and construction**

1. Without prejudice to sections 11 and 23(1) of the Interpretation Act 1978 –
  - (a) these Conditions shall be interpreted and construed in like manner as an Act of Parliament passed after the commencement of the said Act of 1978, and
  - (b) expressions used in these Conditions which are also used in Part I of the Act shall, except where the context otherwise requires, have the same meaning as in that Part.
2. In this Schedule 1 unless the context otherwise requires

“the Act” means the Gas Act 1986;

“Gas Shipping Business” means -

  - (a) shipping activities carried on by the Licensee pursuant to its Gas Shipper licence in arranging with a public gas transporter for gas to be introduced into, conveyed by means of, or taken out of a pipe-line system operated by that transporter for purposes connected with the supply of gas to premises in Great Britain;
  - (b) ancillary activities carried on by the Licensee reasonably related to the shipping and supply activities referred to in sub-paragraph (a) above;
  - (c) commercial and administrative activities to the extent that they are undertaken by the Licensee for the purpose of the activities referred to in subparagraph (a) above including -
    - planning;
    - purchasing and stores;
    - marketing and selling;
    - accounting and finance;
    - personnel management; and
    - any other general management and administrative activities,provided that where the Director is satisfied that any such activity should not properly be treated as part of the Gas Shipping Business, the Director may issue directions to that effect and the activity so specified shall cease to be treated as part of the Gas Shipping Business from the date of issue of the directions or such other date as may be specified in the directions;

“related person” means -

- (a) in relation to an undertaking within the meaning of section 259 of the Companies Act 1985 (“the principal undertaking”), a parent or subsidiary undertaking of the principal undertaking or a subsidiary undertaking of a parent undertaking of the principal undertaking, in each case within the meaning of section 258 of that Act, and
  - (b) in relation to any person (including such an undertaking), a connected person of that person within the meaning of section 286 of the Taxation of Chargeable Gains Act 1992.
3. Where the Licensee is required by these Conditions to do anything within a specified period or by a specified time but fails to do so, that requirement shall continue to have effect after the expiry of that period or after that time without prejudice, however, to any consequence of its not having done that thing within the specified period or by the specified time.
  4. The provisions of section 46(1) of the Act shall have effect as if set out herein and as if for the words “this Part or regulations made under this Part” there were substituted “these Conditions”.
  5. Anything required by or under these Conditions to be done in writing may be done by facsimile transmission of the instrument in question or by other electronic means and, in such case -
    - (a) the original instrument or other confirmation in writing shall be delivered or sent by pre-paid first-class post as soon as is reasonably practicable, and
    - (b) where the means of transmission had been agreed in advance between the parties concerned, in the absence of and pending such confirmation, there shall be a rebuttable presumption that what was received duly represented the original instrument.
  6. Any reference in these Conditions to -
    - (a) a provision thereof;
    - (b) a provision of the standard conditions;
    - (c) a provision of the standard conditions of Public Gas Transporters’ Licences

shall, if these or the standard conditions in question come to be modified, be construed, so far as the context permits, as a reference to the corresponding provision of these or the standard conditions in question as modified.

**Condition 2: Separate accounts for Gas Shipping Business**

1. This condition applies for the purpose of ensuring that the Licensee maintains accounting and reporting arrangements which enable separate accounts to be prepared for the Gas Shipping Business showing the financial affairs of that businesses.
2. The Licensee shall:

- (a) keep proper books of account and records in such a form that the revenues and costs, assets and liabilities of, or reasonably attributable to, the Gas Shipping Business are separately identifiable in the books of the Licensee from those of any other business of the Licensee;
  - (b) so far as is reasonably practicable, prepare for the Gas Shipping Business on a consistent basis from its accounting records in respect of the period from 1 April 1999 to 31 December 1999 and for each succeeding financial year accounting statements comprising -
    - (i) a profit and loss account;
    - (ii) a statement of assets and liabilities with the details reasonably necessary to reconcile the net assets shown in that statement at the beginning and end of the period to which it relates, and
    - (iii) a cash flow statement for the period with a reconciliation to the accounting statements specified in subparagraphs (i) and (ii).
3. The accounting statements prepared under paragraph 2(b) shall -
- (a) set out and fairly present the costs (including depreciation), revenues, assets employed and liabilities of, or as may be reasonably attributable to, the Gas Shipping Business and show separately and in appropriate detail the amount of any revenue, cost, asset or liability which has been either -
    - (i) charged from or to any other business of the Licensee or of a related company of the Licensee; or
    - (ii) determined by apportionment between the Gas Shipping Business and any other business of the Licensee or of a related company of the Licensee; or
    - (iii) charged between the Gas Shipping Business and any other business of the Licensee or any business of a related company of the Licensee;
 together with a description of the basis of the charge or apportionment;
  - (b) so far as is reasonably practicable (if the Licensee is a company required to prepare annual accounts) -
    - (i) have the same content in respect of the business to which they relate as the annual accounts of the Licensee prepared in accordance with the Companies Act 1985 or, in the case of a company incorporated in a country or territory outside Great Britain, in accordance with the law of that country or territory, and
    - (ii) be prepared in accordance with the general rules and format and use the accounting principles and rules applicable to those accounts;
  - (c) state the accounting policies used, and
  - (d) where they do not comply with accounting principles generally accepted in the United Kingdom or in any other country or territory within the European Economic Area, and the Director so directs, be

accompanied by further statements which (notwithstanding anything in sub-paragraph (b)) do comply with principles so accepted,

and any question arising under sub-paragraph (d) as to whether statements comply with the accounting principles there mentioned shall be determined by the Director.

4. Except in so far as the Director accepts otherwise, the Licensee shall not change any basis of charge or apportionment used in the accounting statements in respect of the Gas Shipping Business for any financial year of the Licensee subsequent to the first financial year from the basis used in the accounting statements in respect of that business for the first financial year or, as the case may be, the preceding financial year.
5. The Licensee shall procure, in respect of each set of accounting statements prepared under paragraph 2(b), a report by an appropriate auditor which is addressed to the Director and states whether in his opinion that set of accounting statements -
  - (a) is adequate for the purposes of paragraph 1 and is in compliance with this condition, and
  - (b) represents a true and fair view of the revenues, costs, assets and liabilities of, or reasonably attributable to, the Gas Shipping Business.
6. The Licensee shall furnish the Director with a copy of each set of accounting statements and the auditor's report relating thereto required by paragraphs 2(b) and 5 as soon as is reasonably practicable and in any event not later than 6 months after the end of the period in respect of which the statements are prepared.
7. Subject to paragraph 8 below, the Licensee shall publish each accounting statement required by paragraph 2(b) in such a manner as, in the reasonable opinion of the Licensee, will secure adequate publicity for it and so publish it not later than -
  - (a) the time of publication of the annual accounts of the Licensee for the financial year of the Licensee to which the statements relate, or
  - (b) 6 months (or such longer period as the Director may accept) after the end of that financial year,whichever is the earlier.
8. Paragraph 7 shall not require the publication of the amount or basis of any charge or apportionment to be shown separately under paragraph (3)(a)(i) or (ii) where publication would or might seriously and prejudicially affect the interests of the Licensee, and for this purpose the Licensee shall (except in so far as the Director consents to the Licensee not doing so) refer for determination by the Director any question as to whether any such publication would or might so affect the interests of the Licensee.
9. In this condition—

“appropriate auditor” means, in the case of a Licensee which is a company within the meaning of section 735 of the Companies Act 1985, a person appointed as auditor under Chapter V of Part XI of that Act, in the case of any



other Licensee which is required by the law of a country or territory within the European Economic Area to appoint an auditor under provisions analogous to Chapter V of Part XI of that Act, a person so appointed and, in any other case, a person who is eligible for appointment as a company auditor under sections 25 and 27 of the Companies Act 1989;

“financial year” means a year commencing on 1<sup>st</sup> January; and

references to costs or liabilities of, or reasonably attributable to the Gas Shipping Business shall be construed as excluding taxation, capital liabilities not related solely to that business and interest thereon; and references to a profit and loss account or cash flow statement shall be construed accordingly.

### **Condition 3: Conduct of Gas Shipping Business**

1. The Licensee shall conduct its Gas Shipping Business in the manner best calculated to secure that neither the Licensee or any such person as is mentioned in paragraph 5 obtains any unfair commercial advantage from being related directly or indirectly to any gas transportation business of any such person as is mentioned in paragraph 5.
2. Subject to paragraph 4 below, the Licensee shall use its best endeavours to secure that no information derived from any gas transportation business of any such person as is mentioned in paragraph 5 is used for the benefit of its Gas Shipping Business.
3. Subject to paragraph 4 below, the Licensee shall use its best endeavours to ensure that no information relating to or derived from any gas transportation business conducted by any such person as is mentioned in paragraph 5 is sought from that business by any person engaged in the Gas Shipping Business.
4. Paragraphs 2 and 3 shall not apply in so far as -
  - (a) the Director so consents;
  - (b) a gas shipper or gas supplier has, for the purposes hereof, consented in writing to the use or disclosure of information relating to that shipper or supplier;
  - (c) it is necessary or expedient that the information be used or disclosed to enable the Licensee to enter into transportation arrangements with any public gas transporter or to enter into arrangements related to the storage of gas by any person or to give effect to such arrangements;
  - (d) the information has been published or is required to be disclosed in pursuance of any other condition of this licence; or
  - (e) the information (otherwise than in consequence of a contravention of any condition of this licence) is in the public domain.
5. The persons referred to in paragraphs 1, 2 and 3 are -
  - (a) any related person of the Licensee, and
  - (b) without prejudice to sub-paragraph (a), where the Licensee is a body corporate, any body corporate in which the Licensee or any holding

company or any subsidiary of the Licensee, or any holding company of such undertaking, within the meaning of section 736 of the Companies Act 1985, has a participating interest, within the meaning of section 260 of that Act.

6. The Licensee shall take all reasonable precautions against the risk of failure to comply with paragraphs 2 and 3 including -
  - (a) restrictions on the communication of information to persons engaged in the Gas Shipping Business from any gas transportation business of any such person as is referred to in paragraph 5;
  - (b) restrictions on access by persons engaged in the Gas Shipping Business to-
    - (i) premises or parts of premises occupied for the purpose of any gas transportation business of any such person as is referred to in paragraph 5, and
    - (ii) recorded information relating to any gas transportation business of any such person as is referred to in paragraph 5;
  - (c) the prevention (so far as the Licensee can require it) of any person who has ceased to be engaged in the Gas Shipping Business from being engaged in any gas transportation business of any such person as is mentioned in paragraph 5 until the expiry of the appropriate period since he ceased to be engaged in the Gas Shipping Business.
7. The Licensee shall ensure that –
  - (a) at all times it employs a competent person (hereafter referred to as “the Compliance Officer”) for the purpose of facilitating compliance by the Licensee with this Condition;
  - (b) it consults the Director before employing any person as the Compliance Officer, and
  - (c) the Compliance Officer is provided with such staff and facilities as he may reasonably require to perform the tasks assigned to him pursuant to this condition

provided that for as long as the Licensee is a related person of BG plc the Licensee may employ for the purposes of paragraphs (a) and (c) the persons who are so employed by BG plc.

8. The Licensee shall assign the following tasks to the Compliance Officer-
  - (a) the establishment of procedures, after consulting the Director, for ensuring compliance with this condition;
  - (b) the investigation of any matter which is the subject of a representation made by a gas shipper, public gas transporter or gas supplier that the Licensee may be contravening any paragraph of this condition or that the procedures established under sub-paragraph (a) are not being complied with or are defective;
  - (c) the giving of advice to directors and employees of the Licensee or any such person as is referred to in paragraph 5 for facilitating compliance with this condition and the procedures established under sub-paragraph

- (a) and, in particular, as to whether any information is information to which paragraph 2 or 3 applies;
  - (d) the giving of information or advice as to the procedures established under sub-paragraph (a) to any gas shipper, public gas transporter or gas supplier requesting it.
9. The Licensee shall, as soon as practicable after the end of each financial year, furnish to the Director and publish in such form and manner as the Director may direct, a comprehensive report on the Compliance Officer's activities during that year.
10. In paragraph 6(c) "the appropriate period" means -
- (a) a period of 3 months, or
  - (b) such shorter or longer period as, following a recommendation by the Compliance Officer, the Director may direct in respect of any person or class of persons.

\*\*\*\*\*

**SCHEDULE 2**  
**to the**  
**Gas Shipper Licence granted under section 7A(2) of the Gas Act 1986 to**  
**BG Gas Services Limited**

**MODIFICATIONS TO THE STANDARD CONDITIONS**

**NO MODIFICATIONS TO THE STANDARD CONDITIONS**

**SCHEDULE 3**  
**to the**  
**Gas Shipper Licence granted under section 7A(2) of the Gas Act 1986 to**  
**BG Gas Services Limited**

**REVOCAATION CONDITIONS**

1. The Director may at any time revoke this Licence by the requisite period of notice in writing given to the Licensee in any of the following circumstances-
  - (a) if the Licensee agrees in writing with the Director that this licence should be revoked;
  - (b) if any amount payable under Condition 17 of the Standard Conditions is unpaid 30 days after it becomes due and remains unpaid for a period of 14 days after the Director notifies the Licensee that the amount is overdue, such notification not to be given earlier than the sixteenth day after the day on which the amount payable became due;
  - (c) if the Licensee fails to comply with a final order (within the meaning of section 28 of the Act) or a provisional order (within the meaning of that Section) which has been confirmed under that section and such failure is not rectified to the satisfaction of the Director within 3 months after the Director has given notice in writing of such failure to the Licensee provided that no notice under this sub-paragraph shall be given by the Director before the expiration of the period within which an application under section 30 of the Act could be made questioning the validity of the final or provisional order or before any such application, if made, is finally adjudicated upon;
  - (d) if the Licensee fails to comply with any order made by the Secretary of State under section 56, 73, 74, or 89 of the Fair Trading Act 1973 or section 10 of the Competition Act 1980 which relates to the activities authorised by this Licence;
  - (e) if the Licensee ceases to carry on its business as a gas shipper;
  - (f) if the Licensee shall not have commenced business as a gas shipper within the period of three years from the date on which the Licence takes effect;
  - (g) if the Licensee
    - (i) is unable to pay its debts (within the meaning of section 123 (1) or (2) of the Insolvency Act 1986), but subject to paragraph 2 below) or it has any voluntary arrangement proposed in relation to it under section 1 of that Act or makes a composition or scheme of arrangement (other than for the purpose of a reconstruction or amalgamation upon terms and within such period as may previously have been approved by the Director);

- (ii) has a receiver (which expression shall include an administrative receiver within the meaning of section 29 of the Insolvency Act 1986) of the whole or any material part of its assets or undertaking appointed;
- (iii) becomes subject to an administration order under section 8 of the Insolvency Act 1986;
- (iv) passes any resolution for winding up other than a resolution previously approved in writing by the Director;
- (v) becomes subject to an order by the High Court for winding up.

2. For the purposes of sub-paragraph 1(g)(i) of this Schedule, section 123(1)(a) of the Insolvency Act 1986 shall have effect as if for “£750” there was substituted “£10,000” or such higher figure as the Director may from time to time determine and the said section 123(1)(a) shall not apply if the demand referred to is being contested in good faith by the Licensee with recourse to all appropriate measures and procedures or if the demand is satisfied prior to the expiry of the notice given by the Licensee to the Director.

3. The requisite period of notice shall be-

- (a) for the purposes of sub-paragraph 1(g), 24 hours: and
- (b) for all other purposes, 30 days.

\*\*\*\*\*

## Letter to BG plc

As you were advised just before Easter, Ofgas has decided to grant a gas shipper's licence to BG Gas Services Ltd (GSL). The licence includes the special conditions proposed in our consultation paper and has been sent to you by our licensing section.

Ofgas indicated at that time that it would write to BG plc in connection with the grant of the licence, making clear from the outset its policy in relation to the application of the special and other relevant conditions of the BG plc and GSL licences. We want to make that policy entirely clear to you for two reasons. Firstly, although the Gas Act 1986 does not prohibit companies in the same group from having both public gas transporter and gas shippers licences, we have an underlying concern about such grants, particularly when one of the licence holders has dominance in the conduct of its licensed activities, as BG plc is assumed to have in gas transportation. There is clearly a risk of unfair commercial advantage and it is because of this that special conditions have been included in the GSL licence.

Secondly, these concerns have been reinforced by the consultation exercise that has occurred. Our decision document following that exercise is enclosed and separate arrangements are in hand to ensure that both BG plc and GSL have copies of all the representations made in response to the consultation paper except one which was confidential.

Ofgas therefore will want to ensure that the relevant standard and other conditions in both licences are observed and are seen to be observed. You should expect that, apart from relying on the activities of the Compliance Officer, Ofgas will use the conditions of both licenses relating to the provision of information to satisfy itself as to observance. Ofgas also will look to BG plc to ensure that the Compliance Officer's work is thoroughly conducted and fully reported.

Specifically, we regard the separation of premises and computer systems as necessary for BG plc to comply with Standard Condition 11 of its licence and for GSL to comply with Special Condition 3 of its licence. We will look closely at the apportionment of the cost of common services. We also regard the maintenance of an accurate audit trail for all transactions between GSL and Transco as necessary to demonstrate compliance with these licence conditions. In this regard, you have agreed to supply Ofgas with details of all transactions in the flexibility mechanism undertaken by GSL

I shall be grateful if you will acknowledge receipt of this letter.

JUSTIN COOMBS  
**Director of Transportation Regulation**

**List of Respondents to the Consultation Document**

British Gas Trading Ltd (on behalf of itself and Centrica plc) (BGT)

Eastern Group (Eastern)

Gas Consumers' Council (GCC)

Health and Safety Executive (HSE)

Mobil Gas Marketing (UK) Ltd (Mobil)

Scottish and Southern Energy plc (SSE)

Scottish Power (SP)

United Gas Services Ltd (United)

Northern Electric & Gas Ltd (Northern)

(Plus one confidential response)



## Summary of Adverse Objections and Representations

	Objection/Representation	Company	Ofgas Response
<b>a) Should GSL be granted a gas shipper's licence?</b>			
1	Any future application for a supply licence to be subject to consultation.	BGT	Agreed.
2	The argument that a licence should be granted because the Gas Act does not proscribe it is weak.	Eastern	Ofgas disagrees: although Ofgas has some discretion, it can only refuse to grant a licence if . . . . It must also be satisfied that special conditions could not overcome these problems. Ofgas concluded in this case that special conditions would be sufficient.
3	The grant of a shipping licence to a business related to the dominant PGT is of a different order of magnitude to the grant of licences to independent PGTs associated with gas shippers.	Eastern	Ofgas agrees and is seeking to reflect the differences in the special conditions included in the shipping licence of GSL, together with the special and amended standard conditions of the Transco licence.
4	Ofgas must act in the best interests of consumers and of competition.	Eastern	Ofgas agrees with this point and is seeking so to act.
5	The application is analogous to NGC seeking to purchase and operate generation capacity.	Eastern	BG is different to NGC because it already owns an exploration and offshore production business.
6	Ownership of the pipe-line and a shipping business causes an inherent conflict of interest that is best dealt with by de-merger	United	Ofgas sees the logic of this argument, but doubts if having a shipping business gives rise to additional difficulties over and above those deriving from ownership of E&P. Ofgas sees licence conditions as the best way of dealing with conflicts in the absence of de-merger

<b>b) Has Ofgas correctly identified the potential anti-competitive arrangements?</b>			
7	Granting a shipper licence provides an opportunity for BG group "guidance" for overall commercial success.	BGT	This is a danger; Ofgas thinks that it is best addressed by granting a licence to GSL with appropriate special conditions and by reliance on the conditions in the Transco licence.
8	Potential for distortion in market for shipping services.	BGT	Should be addressed through special condition 3 of GSL licence and standard condition 11 of Transco licence.
9	Preferential access to network, particularly in relation to capacity.	BGT	Should be addressed through special condition 3 of GSL licence and standard condition 11 of Transco licence. Move to auctions proposed in RGTA should also address this.
10	Possible distortions in interruptible market.	BGT	Should be addressed through special condition 3 of GSL licence and standard condition 11 of Transco licence.
11	Information should neither be provided by Transco nor sought by GSL.	BGT	Addressed by special condition 3.3 of GSL licence and standard condition 11(8) of Transco licence.
12	Requirements that exist to restrict transfer of staff to be re-established.	BGT	Addressed in special condition 3.6 of GSL licence; Ofgas believes that current requirements are being followed but will review the matter.
13	There is an incentive for Transco to accept flexibility bids nominated by GSL.	Eastern	Special condition 3 of the GSL licence and standard condition 11 of the Transco PGT licence are intended to counter this incentive.

14	Ofgas has not identified the full extent of the risks. The current disadvantage to BG's E&P business is more than outweighed by potential disadvantage to other producers and shippers.	Eastern	The weight of responses suggests that BG's E&P business of itself gives advantages to BG. The E&P business will continue whether or not GSL is granted a licence. With GSL licensed Ofgas has more regulatory controls than if GSL is not granted a licence.
15	Incentive to bid up Transco or BG Storage services to enhance the overall BG plc financial position.	SP	Noted. This is the purpose of the licence conditions requiring both Transco and GSL to conduct their operations in the manner best calculated to ensure that they and related companies obtain no unfair commercial advantage.
16	Indirect anti-competitive actions need to be addressed, including those deriving from single executive control under the BG plc board and the restricted environment in which BG and its subsidiaries operate.	United	See responses to points 2 and 18 above.
17	GSL will have a knowledge advantage compared to other shippers because of its easier access to Transco employees; other organisations will have to pay a premium to attract BG employees.	United	If staff can command a salary premium, BG will also have to pay this premium to retain staff. In practice, however, BG has been decreasing its workforce, giving rise to an availability of experienced personnel on the labour market.
<b>c) Was Ofgas correct in its view that no additional conditions were required in BG's PGT licence?</b>			
18	Obligations should be on the monopoly and not on competitive activities	Eastern	Transco is already subject to licence conditions.
19	Transco's PGT licence should also contain provisions relating to the occupation of by GSL and Transco of the separate premises.	Eastern	Amended Standard Condition 11 of BG's PGT licence covers this.

<b>d) Are the proposed special conditions necessary and sufficient to address these potentially anti-competitive arrangements?</b>			
20	GSL should be required to provide Ofgas with its bid strategy for the flexibility mechanism; bidding/purchasing strategies must be justifiable on economic grounds.	BGT; SP	Agreed. To be progressed through special condition 3 of GSL licence.
21	The access-to-premises restriction may not be sufficient; separation of computer systems may be required; staff in Transco and GSL must be prevented from sharing accommodation to avoid the risk of inappropriate transfer of information.	BGT	Ofgas will follow this up through special condition 3 of the GSL licence.
22	Separation at BG board level of Transco and GSL interests needs to be addressed.	BGT	It is impossible to achieve completely distinct decision-making processes at BG board level for Transco and GSL. However, Ofgas is confident that there is at BG board level an appreciation of the importance of not risking the revocation of either licence and that the introduction of special conditions therefore will be an effective disincentive to anti-competitive behaviour within the BG group.
23	Role of Compliance Officer needs to be extended.	BGT	Ofgas believes that the licence conditions that have been introduced give the Compliance Officer the correct obligations. Ofgas recognises that it is important that these obligations are followed and are seen to be followed.
24	Need to establish an adequate audit trail of trades between Transco and GSL.	BGT	Agree.
25	Special obligations on GSL are a "belt and braces" solution of little benefit.	SSE	Ofgas thinks that obligations are required in both licences, so that enforcement action could be taken against both BG and GSL.

**Other Points**

26	Seven days for consultation is unsatisfactory.	GCC; Mobil	Ofgas agrees. Part of the reason for the short consultation period is internal delay by Ofgas as recent reorganisation decisions have had to be taken. We regret the short period and we are endeavouring to avoid such short periods in the future.
----	--	------------	--