



Shippers, Transco, UKOOA
and Other Interested Parties

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value to customers*

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Dear Colleague,

Access to offshore information

Consultation on a possible derogation to Standard Condition 4E of Transco's Gas Transporters Licence

You may know that the Department of Trade and Industry (DTI) has been facilitating discussions with the UK Offshore Operators Association (UKOOA), Transco and Ofgem to improve the flow of information from the offshore gas producers to Transco and to the onshore gas market. The DTI has explained that offshore gas producers representing over 95% of UK production have now committed themselves to an increased flow of information, on a voluntary basis, provided that the detailed underlying data, which they consider to be commercially confidential, is protected by a confidentiality agreement with Transco. While Ofgem has supported this process and welcomes the progress that has been made, we consider that the confidentiality agreement being proposed between Transco and the producers could give rise to a breach of Transco's Gas Transporters (GT) licence. National Grid Transco has made it clear that they would be unwilling to sign such an agreement if such an action could later place them in breach of their GT licence (e.g. when a modification proposal to its network code was raised).

In connection with this exercise, Ofgem is today commencing a short consultation on whether to issue a temporary informal derogation ("derogation") to standard condition 4E of Transco's GT licence. Such derogation could help to enable Transco to enter into the proposed confidentiality agreement with gas producers without the risk of breaching its GT licence.

Rationale for information disclosure

In recent years, some market participants, including customers and shippers, have raised concerns about their limited access to offshore information. They also consider that their position in the wholesale gas market could have been compromised by other market participants, in particular those with offshore affiliates, having access to better information. In addition, Transco has indicated that the operational uncertainties that it faces in predicting gas flows on the day are exacerbated by its inability to access reliable offshore maintenance and outage information both ahead of the day and within day.

Ofgem shares these concerns and considers that the disclosure of offshore information can improve the operation of the wholesale gas market in a number of ways:

- ◆ A lack of information to Transco can result in it taking unnecessary actions to balance gas inputs to and offtakes from the transmission system, imposing unnecessary costs on the market (and ultimately customers).
- ◆ A lack of information to market participants reduces their ability to react to and address supply shortfalls. As a result, more reliance is placed on Transco to address such shortfalls, increasing the costs of operating the system.
- ◆ At its extreme, the inability of prices to adjust in response to supply (and demand) conditions, due to an absence of offshore information, may exacerbate the risk of security of supply incidents. In particular, if Transco and other market participants are not aware of a supply shortfall there may be insufficient time to source gas which, in turn, may increase the likelihood of a gas emergency.
- ◆ Participants who have access to offshore information through their offshore affiliates could be at a competitive advantage compared to those without offshore affiliates.
- ◆ Consistent with the operation of the electricity market, Ofgem considers that greater information provision should lead to a more efficient gas market¹.
- ◆ In June 2003, Transco initiated interruptions of National Transmission System (NTS) and Local Distribution Zone (LDZ) supply points under interruptible transportation contracts as a result of supply deficits in the south of Great Britain. The subsequent review of the events surrounding these interruptions indicated that, amongst other contributing factors, improved information flows between offshore and onshore gas industries could have enhanced Transco's abilities to manage the system.
- ◆ In October 2003, NGT indicated in its Winter Operations Report 2003/4² that the delivery of beach gas would be critical to ensure overall security of supply in the event of a severe winter this year. We understand that NGT's concerns have been confirmed by observed beach flows during this Winter.

¹ In the electricity market, analogous information is given to NGC and the market by generators as a result of licence obligations, ie such information provision is not voluntary.

² *Winter Operations Report – 2003/2004*, National Grid Transco, 14 October 2003

The offshore information disclosure project

In mid 2003, the DTI initiated detailed high level discussions to put in place a voluntary information disclosure arrangement from the offshore community to Transco and the wider market. In that light, Ofgem has worked closely with the DTI, UKOOA and Transco to facilitate the disclosure of offshore information to Transco and other market participants. It was agreed during these discussions that information disclosure would be discussed and implemented in a phased approach.

The DTI considers that there is scope for greater offshore information provision and supports a voluntary arrangement for such disclosure. The DTI indicated, however, that a failure to reach voluntary agreement could lead it to pursue a legislative solution. Ofgem has supported the DTI's views and would support either a voluntary agreement or a legislative approach (albeit that Ofgem would prefer a legislative route).

As result of these discussions, in November 2003, agreement was reached on the first phase to improve and standardise information provided to Transco on gas flows, and planned and unplanned outages. It was also agreed that in the event of a potential gas emergency, Transco will request that the DTI obtain maximum deliverability information from offshore participants on Transco's behalf. A voluntary agreement between offshore companies and DTI was put into effect on 11 November 2003. We understand that the provision of information flowing to Transco has improved as a result of this agreement.

A possible agreement has now been reached with the gas producers on phases two and three. Phase two seeks the disclosure of operational and planning information which Transco uses for long term planning purposes. Transco also uses this information to publish its 'Ten Year Statement'³. In order to facilitate the disclosure of information for the Ten Year Statement, it has been proposed that Transco sign an agreement with offshore participants to address issues of confidentiality and liability. Inter alia, the proposed agreement contained a provision that should a modification be proposed to Transco's network code which required the disclosure of information protected by the agreement, offshore information could be recalled by the producers, or destroyed by Transco on request of the producers.

Phase three proposes the disclosure of aggregated information to all market participants including, in particular, customers. This information is:

- National and zonal⁴ near to real time flows onto the NTS
- National and zonal ahead of and during day forecast flows onto the NTS
- National and zonal forecast deliverability reflecting planned maintenance
- After the day flows into the NTS by sub terminal (this information is already available to gas shippers).

Condition 4E of the Gas Transporter's licence and UKOOA's concerns

³ The Ten Year statement is published by Transco under the title "Transporting Britain's Energy".

⁴ The boundaries for zonal information are as yet undecided. However it is the current working assumption that there would be two zones.

UKOOA has raised concerns with regard to the disclosure of phase two information with respect to confidentiality. In particular, it is concerned that confidential information on individual fields which producers provide to Transco for the Ten Year Statement could be made available to all market participants by virtue of Condition 4E of Transco's GT licence.

Section 5 of Condition 4E requires Transco to comply with any obligation in its network code to disclose information relating to the operation of Transco's pipeline system or any market relating to the licensee's pipeline system. The guidance notes issued at the time section 5 of Condition 4E was proposed as a licence change clearly envisaged that information from offshore companies could fall within the scope of the licence condition. Section 5 of Condition 4E was consulted upon during 2001 and 2002. There was broadly a balance between those who supported and opposed the licence condition with a slight majority in favour of the licence condition. The Secretary of State did not veto the licence condition and, as such, it was implemented as part of the Transco price control and SO incentives 2002-7⁵. The relevant extract from Transco's licence is attached as appendix one.

During the consultation, UKOOA sought assurances from Ofgem that information provided to Transco on a confidential basis would not be disclosed to the wider market. In particular, it was concerned that shippers and designated third parties could raise a network code modification proposal to disclose information that had been provided to Transco relating to individual commercial positions.

To alleviate these concerns, Ofgem set out some guidance⁶ on the criteria it would use to determine whether to approve a network code modification requiring the disclosure of information. In particular, Ofgem noted that in deciding whether to implement a network code modification, consideration would need to be given as to whether the proposal better facilitates the relevant objectives⁷ of Transco's network code. Ofgem considered that a proposal which required Transco to breach confidentiality obligations to third parties to its network code or was likely to result in such third parties withholding information hitherto provided to Transco on a voluntary basis would be unlikely to fulfil that criterion.

During the development of the voluntary arrangements, Ofgem offered further clarification of the circumstances in which the licence condition could be used. This was contained in our letter of 23 October 2003⁸. In this letter, Ofgem noted that, generally speaking, the disclosure of ex ante information should be at a level of aggregation which does not disclose an individual participant's commercial position. Ofgem also agreed to formally seek the DTI's views on any modification proposal relating to the disclosure of potentially confidential information by Transco to the industry prior to reaching any decision. Nevertheless, it is clear that Ofgem could not fetter its discretion with regard to any prospective modification proposals.

⁵ *Transco Price Control and SO incentives 2002-7 – Licence modifications and way forward*, Ofgem, 27 September 2002

⁶ *Transco Price Control and SO incentives 2002-7, Explanatory notes to accompany the section 23 notice of proposed modifications to Transco's gas transporter licence*, Ofgem, April 2002

⁷ Transco's relevant objectives are attached as appendix two

⁸ *The disclosure of offshore information*, Ofgem open letter, 23 October 2003

UKOOA welcomed the clarification that this letter brought. However, UKOOA sought unequivocal commitment from Ofgem that it would not approve a network code modification to disclose field specific confidential information agreed to in phase two. Without this commitment from Ofgem, UKOOA was of the view that it would be unable to agree to the voluntary disclosure of phase two information.

The derogation

Ofgem is committed to working with the DTI to facilitate a voluntary agreement for the disclosure of offshore information. Ofgem has noted UKOOA's ongoing concerns with regards to confidentiality and considers that it would be unable to provide further assurances on how it would treat any prospective modification proposals since Ofgem could not fetter its discretion as to whether to direct the implementation of any modification proposal. However, in order to facilitate a voluntary agreement, Ofgem has considered consulting on an amendment to Condition 4E of Transco's GT licence

With respect to an amendment to Condition 4E of Transco's GT licence, the appropriate procedure would be to commence a formal consultation to consider amending Condition 4E of Transco's GT licence. However, given Ofgem's statutory requirement to consult on a licence amendment this would take several months. Moreover, Ofgem is mindful of the timing of pending energy legislation as well as the need to bring the voluntary arrangements into effect as soon as possible so as to contribute to Transco's forthcoming Ten Year Statement which is now in preparation.

DTI has made clear that in the absence of a voluntary agreement on disclosure of gas information it would need to consider legislation. However the DTI prefers a voluntary approach, if this can be reached, in order not to increase, unnecessarily, the burden of regulation on the industry. If, in the absence of this derogation, it proved impossible to implement the voluntary arrangements that have been agreed with the offshore gas industry the DTI would need to consider all the options. In this respect, DTI would recognise the willingness that the industry has shown to pursue the voluntary route and there can be no presumption that early legislation would follow.

In light of the exceptional circumstances that prevail and in order to facilitate the voluntary agreement Ofgem is considering whether to issue a temporary derogation to Condition 4E of Transco's GT licence. As there is no statutory basis or basis in licence to enable the grant of any formal derogation or direction, such a derogation could be granted by Ofgem only on an informal basis.

The suggested derogation, if agreed, would preclude Transco from complying with a network code modification to disclose information which could potentially reveal an individual participant's commercial position arising from the disclosure of phase two information. For clarification, phase two information is information provided to Transco from offshore participants for the purposes of publishing the Ten Year Statement.

The suggested derogation, if agreed, would automatically expire six months from the date of grant and in this time Ofgem would formally consult on whether Condition 4E should be amended. The grant of any such temporary derogation would be entirely without prejudice to any later statutory consultation on amendment to Condition 4E of Transco's GT licence.

However, if as a result of this consultation, Ofgem concluded that an informal derogation was not appropriate, it would seem that reliance would continue to be placed upon the letter of 23 October 2003, and the guidance given in the original licence condition consultation. Alternatively, as explained above, the DTI could decide to seek a legislative solution to ensure the disclosure of offshore information.

Way Forward

In the event that Ofgem decides to issue a temporary derogation to Condition 4E of Transco's GT licence, following due consideration of respondent's views, Ofgem would expect UKOOA and Transco to be in a position to agree to the voluntary disclosure of phase two information soon thereafter and, in particular, to sign the confidentiality agreement that has been proposed.

Alternatively if, as a result of this consultation, Ofgem determines that a derogation is inappropriate, the DTI has indicated that it considers that the current agreement with the gas industry on the voluntary disclosure of information would not be capable of implementation.

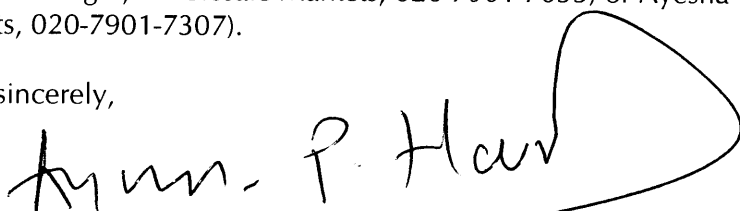
Views Invited

Ofgem is now seeking views from industry participants on whether it is appropriate to issue a temporary derogation to Condition 4E of Transco's GT licence by 31 March 2004. You can write to the address above or send electronic responses to kyran.hanks@ofgem.gov.uk. Given the involvement of the DTI in this matter, it would be helpful if replies were copied directly to the DTI, Valerie.Haines@dti.gsi.gov.uk

Responses will be placed in the Ofgem library unless marked confidential. The short consultation period is driven by the need for Ofgem to reach a view on whether to implement a derogation before opportunity to seek a legislative solution, via the Energy Bill, expires. In making this decision, Ofgem is mindful that significant consultation has already taken place on the implementation of Condition 4E of the GT licence.

If you have any questions regarding this letter do not hesitate to contact me, Samanta Padalino (Senior Manager, Wholesale Markets, 020-7901-7033) or Ayesha Uvais (Manager, Wholesale Markets, 020-7901-7307).

Yours sincerely,



Kyran P Hanks
Director, Wholesale Markets

Appendix one: Extract from Amended Standard Condition 4E of Transco's GT licence

" 5. The licensee shall comply with any obligation in the Network Code to disclose information relating to:

- (i) the operation of the licensee's pipe-line system; or
- (ii) any market relating to the licensee's pipe-line system"

Appendix two: Transco's relevant objectives

Extract from Condition 9 of Transco's GT licence

1. The licensee shall establish transportation arrangements in respect of matters other than those to which standard conditions 4 (Charging Gas Shippers - General) and 4A (Obligations as Regards Charging Methodology) relate which are calculated, consistently with the licensee's duties under section 9 of the Act, to facilitate the achievement of the following objectives –

- (a) the efficient and economic operation by the licensee of its pipe-line system;
- (b) so far as is consistent with sub-paragraph (a), the efficient discharge of its obligations under this licence;
- (c) so far as is consistent with sub-paragraphs (a) and (b), the securing of effective competition between relevant shippers and between relevant suppliers; and
- (d) so far as is so consistent, the provision of reasonable economic incentives for relevant suppliers to secure that the domestic customer supply security standards (within the meaning of paragraph 4 of standard condition 32A (Security of Supply – Domestic Customers) of the standard conditions of Gas Suppliers' licences) are satisfied as respects the availability of gas to their domestic customers,

hereinafter referred to as "the code relevant objectives".