



Shippers, National Grid Transco,
UKOOA and Other Interested Parties

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Dear Colleague,

Access to offshore information: Derogation to Paragraph 5 of Amended Standard Condition 4E of Transco's Gas Transporters Licence

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, in its role as System Operator, and to participants in the onshore gas market (including customers). The DTI has indicated that offshore gas producers representing over 95% of UK production have committed themselves to increasing the flow of information, on a voluntary basis, provided that the detailed underlying data is protected by a confidentiality agreement with Transco. Although Ofgem has supported this process, we identified a concern that the proposed confidentiality agreement could lead to Transco being in breach of its Gas Transporters (GT) licence.

Having identified this concern, Ofgem launched a short consultation on 23 March 2004. Ofgem consulted, through an open letter, on whether to issue a temporary informal derogation (derogation) to paragraph 5 of amended standard condition 4E of Transco's GT licence. The derogation would enable Transco to enter into the proposed confidentiality agreements (as proposed by Transco and identified later in this letter) with producers without the risk of breaching its GT licence. The consultation ended on 31 March 2004.

Ofgem has carefully considered the views of respondents and the issues that were raised in the consultation. Ofgem has now decided to grant this temporary derogation to paragraph 5 of amended standard condition 4E of Transco's GT licence. This derogation will last for 6 months and will be specific to field information collected by Transco for the purposes of producing its long term planning and forecasts, which are published in its Ten Year Statement under the title "Transporting Britain's Energy" (TBE).



Background

Paragraph 5 of Condition 4E of the Gas Transporter's licence

Paragraph 5 of amended standard condition 4E of Transco's GT licence 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. Condition 4E was amended in 2002 with the purpose of progressing the release of additional gas system and market information to all market participants, including customers. The guidance notes¹ issued at the time envisaged that information from offshore companies could fall within the scope of the licence condition. Ofgem consulted on introducing paragraph 5 of Condition 4E during 2001 and 2002. There was broadly a balance between those who supported and opposed the licence condition. The Secretary of State did not veto the licence condition and, as such, it was implemented from April 2002 as part of the Transco price control and SO incentives 2002-7².

The offshore information disclosure project

During summer 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. Summer interruptions had not been experienced previously. There were other incidents when system conditions almost resulted in further interruptions and / or high cost balancing actions by Transco. To some degree, these incidents were attributable to the nature of the information flow between the offshore and onshore gas industries. In particular, Ofgem considered that the provision of more detailed and timely information on terminal and offshore outages that occurred at the time may have helped resolve the supply deficits through normal market mechanisms potentially minimising the need for interruption.

In that light, work was undertaken by the DTI in consultation with UKOOA, terminal operators, Transco and Ofgem to consider the effectiveness of communications and information release between the offshore and onshore gas industries. The DTI concluded that there were improvements that could be made in this area and initiated discussions to put in place a voluntary information disclosure arrangement from the offshore industry to Transco and the wider market. Ofgem has worked closely with the DTI, UKOOA and Transco to facilitate greater disclosure of offshore information to Transco and other market participants. It was agreed that information disclosure would be developed and implemented in a three phased approach.

During these discussions, the DTI has supported a voluntary arrangement for the disclosure of offshore information. However, it has also indicated that a failure to reach voluntary agreement could lead it to pursue a legislative solution to ensure that information was provided to Transco

¹ *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.*

² *Transco Price Control and SO incentives 2002-7 – Licence modifications and way forward, Ofgem, 27 September 2002.*

by the offshore industry. Ofgem made clear that it would prefer that a legislative route was adopted but supported the DTI in seeking to agree a voluntary approach.

On 11 November 2003, a voluntary agreement was put in place 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 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 to produce its TBE forecasts. In order to facilitate the disclosure of this information, it has been proposed that Transco sign an agreement with offshore participants to address issues of confidentiality and liability. 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 ("recall or destroy provision").

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

- national and zonal 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; and
- after the day flows into the NTS by sub terminal (this information is already available to gas shippers).

UKOOA has raised concerns with regard to the disclosure of phase two information. 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.

During the development of DTI's proposals, UKOOA sought assurances from Ofgem that information provided to Transco on a confidential basis would not be disclosed to the wider market. To alleviate these concerns, Ofgem set out some guidance on the criteria it would use to determine whether to approve a network code modification requiring the disclosure of information. In particular, Ofgem wrote a letter on 23 October 2003³ where it noted that, in deciding whether to implement a network code modification, some consideration would be given as to whether the proposal better facilitates the relevant objectives of Transco's network code⁴. In this respect, we 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 provided to Transco on a voluntary basis would be unlikely to fulfil that criterion.

³ *The disclosure of offshore information*, Ofgem open letter, 23 October 2003.

⁴ The relevant objectives of Transco's network code are outlined under standard condition 9 of Transco's GT licence.

In this letter, 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, Ofgem could not fetter its discretion with regard to any prospective modification proposals.

UKOOA welcomed the clarification that this letter brought but said that it needed greater certainty that Ofgem 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. As stated above, Ofgem cannot, as a matter of law, provide such reassurances as it cannot fetter its discretion in respect of any prospective modification proposal.

The derogation

In order to facilitate a voluntary agreement, Ofgem considered consulting on a formal amendment to condition 4E of Transco's GT licence. The amendment, if made, would have allowed Transco to enter into the proposed agreements without risk of licence breach. However, the process required for a formal consultation on a licence amendment would take several months and facilitating the release of more information to Transco quickly is important both for security of supply and facilitating competition in the gas market. Ofgem therefore launched a short consultation on whether to issue a temporary derogation to paragraph 5 of amended standard condition 4E of Transco's GT licence. Ofgem made clear in the consultation letter that the proposed derogation could only be granted on an informal basis as there is no statutory basis or basis in the licence to enable the grant of any formal derogation or direction.

Ofgem proposed that that the derogation would preclude Transco from complying with network code modifications to disclose information arising from the TBE process which could potentially reveal an individual participant's commercial position with respect to field specific information. Further, the derogation would expire six months from the date of grant. 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.

The consultation ended on 31 March 2004. The views expressed by respondents are summarised below. A copy of the non confidential responses has been published today on Ofgem's website at www.ofgem.gov.uk

Respondents' views

Ofgem received 24 responses to the consultation.

The large majority of respondents supported the proposal that Ofgem should issue the derogation as it would facilitate the disclosure of additional information on offshore activities that would bring security of supply benefits and enhance competition in the wholesale gas market.

Some of the respondents qualified their support for the derogation by stating that

- Ofgem and the DTI should monitor the effectiveness of the voluntary agreement to ensure that gas producers are fully complying with its requirements and, in the event of a failure of the voluntary regime, the DTI should pursue the legislative option;
- the legislative route would be preferable as it would provide a long term, more certain, solution to securing greater offshore information provision; and
- this derogation would not represent good regulatory practice, to the extent that it would create ambiguity regarding the exact interpretation of the licence condition for both Transco and offshore producers, and it would also set an unwelcome precedent for other licence conditions.

Only one respondent strongly opposed the proposed temporary derogation on the basis that it was a risky, not adequately assessed, action on an important part of Transco's licence conditions which could jeopardise the general level of information release available to the industry. The respondents strongly supported the legislative route.

Respondents made some additional comments. Some respondents maintained that the derogation should remain in place for longer than six months, ideally until amendments to licence condition 4E or a longer term solution were consulted upon and approved by Ofgem. This would give reassurance to information providers and ensure their full engagement in the 2004 TBE process.

Another respondent commented that although a temporary derogation is one option, a longer term solution could be the appointment of a third party agent to manage offshore information. It was the opinion of this respondent that this could help overcome issues of confidentiality in a manner which could address the concerns and interests of all parties involved.

Some respondents believed that although a legislative route would be preferable, a voluntary agreement represents a pragmatic solution to facilitate rapid progress on the information disclosure debate, whereas legislation will introduce unwanted delays.

Finally, one respondent stated that the licence condition 4E should be removed in its entirety to help improve the functioning of the wholesale gas market.

Ofgem's views

Before setting out the reasons for our decision, we would reiterate that the proposed derogation would be issued on an informal basis as there is no statutory basis or basis in licence to enable the grant of any formal derogation or direction.

Ofgem considers that the release of reliable information on offshore disclosure is critical for the efficient operation of both the wholesale markets and Transco's transmission system. In recent years, market participants, including customers and shippers, have raised concerns about their limited access to offshore information. They considered that their position in the wholesale gas market could have been compromised by other market participants, especially those with offshore affiliates, having access to better information.

Transco has also 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. Improving the flow of offshore information to Transco, in its role as system operator, should therefore enhance security of supply.

Ofgem remains of the view, supported by a number of respondents, that it would be preferable to put in place, through legislation, obligations on offshore producers to provide this information. However, DTI have made clear that they prefer to pursue a voluntary route.

Ofgem also recognises the concerns expressed by one respondent about the risk associated with issuing an informal derogation. Ofgem is satisfied, however, that the proposed approach is reasonable given the specific circumstances surrounding the provision of offshore information and the significant benefits associated with facilitating the provision of greater information to Transco and the wider market,

Ofgem has therefore decided, in the light of the identified benefits and the specific circumstances, to grant a temporary derogation to licence condition 4E of Transco's GT licence. Ofgem believes that such a derogation will lead to enhanced information flow between the producers and Transco, as well as facilitating the release of offshore information to the market. As such, the derogation should improve the efficient functioning of the gas market. The derogation would be limited to field specific information collated by Transco for the purpose of producing its TBE forecasts.

Ofgem recognises that the grant of a temporary informal derogation does not represent a long term solution to ensure a reliable provision of TBE information. We therefore intend to begin consulting on possible amendments to licence condition 4E to deliver a longer term solution to the problem identified. In the meantime, Ofgem will monitor the effectiveness of the voluntary agreement to ensure that Transco's system operations and the market are actually benefiting from it.

Transco has expressed its concerns about the recall and destroy provision in the confidentiality agreement being negotiated with UKOOA. In particular, as outlined above, the proposed agreement currently contains 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. The issuing of a temporary derogation should, in principle, lead to the removal of this provision as it is rendered unnecessary by the derogation. However, Transco has indicated that the companies entering into the agreements may not be satisfied with the removal of such clause. Transco has therefore proposed that the recall and destroy provision remain in the proposed agreement but that the provision can only be invoked within a short window at the end of the derogation period if Ofgem had not granted an extension to the derogation or amended standard condition 4E of Transco's gas transporters licence. Ofgem considers that this is a reasonable approach.

Decision and way forward

Ofgem has decided to grant a temporary derogation to paragraph 5 of amended standard condition 4E of Transco's GT licence. This derogation will last from the date of this letter until

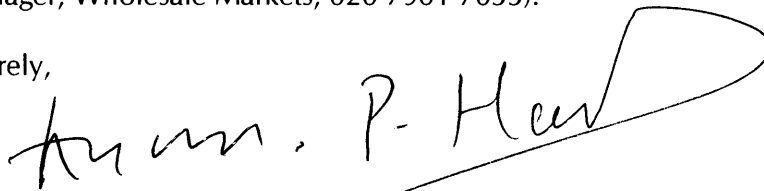
31 October 2004, and is specific to field information collated by Transco for the purposes of producing its long term planning and forecasts, which are published in its Ten Year Statement.

In granting the derogation, Ofgem expects UKOOA and Transco to be in a position to agree to the voluntary disclosure of phase two information immediately hereafter and, in particular, to sign the confidentiality agreement that has been proposed.

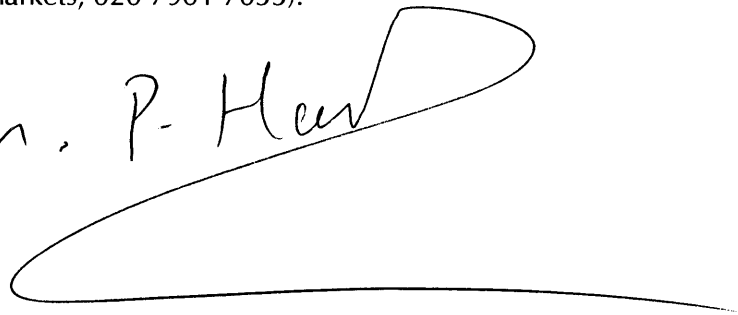
Ofgem expects to begin consulting on possible amendments of paragraph 5 of amended standard condition 4E of Transco's GT licence in due course.

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

Yours sincerely,

A handwritten signature in black ink that reads "Kyran P. Hanks". The signature is written in a cursive style with a large, sweeping loop at the end of the name.

Kyran P Hanks
Director, Wholesale Markets

A large, horizontal, handwritten flourish or signature in black ink, consisting of a long, sweeping line that curves upwards at the end.

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