

14 December 2004

Ms Sonia Brown
Director, Transportation
Office of Gas & Electricity Markets
9 Millbank
London SW1P 3GE

Dear Sonia,

Re: NGT – Potential sale of gas distribution network businesses. Final Impact Assessment 255/04

I am sure you are well aware of my views regarding the proposed sale but I will re-state them for the record.

meuc is a body representing major energy consumers in the industrial and commercial sector. Members' interests are diverse and include Government bodies, the public sector, multi site retail outlets, major food retailers, car manufacturers and many industrial companies covering chemical, cement, paper, engineering and food.

Your document asks respondents to state whether they are in favour of the "sale" or "no sale" option. I am afraid that I find it impossible to give a one line answer to such a complex issue. However if I am forced to make a choice I would say "no sale".

The actual ownership of each DN is almost irrelevant to consumers as they are three steps removed and have no contractual relationship. However consumers tend, like most, to be happy in our comfort zone of "better the devil you know", especially as Transco have proved to be a reliable, if not always innovative, gas Transporter.

I do however have a number of concerns both general and specific which I will share with you.

Eddie Proffitt
Gas Group Chairman

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I will begin with my concern regarding quality of service. As the potential buyers of the DNs have offered considerably more than their asset value it will be necessary for the buyers, if the sale is approved, to make significant savings just to bring them back to the starting line. It is inevitable that cost savings of the magnitude required must equate to less people.

I am happy that the HSE will ensure that the sale of DNs will not put the safety of the system in jeopardy, but safety is not service. I believe that the HSE will be satisfied at site level if the new DN owner matches Transco's response time in isolating a site.

The length of time a site then remains isolated is not relevant to HSE, in fact the less sites connected to the system the safer it becomes. I feel that the task of ensuring that the new DN owners at least match Transco on repairs and reconnections must fall to Ofgem. This I believe must be a pro-active monitoring role as gas consumers will be most unhappy to see a repeat of recent history in the electricity industry. The delay associated with DNOs flying engineers in from their parent companies in Scotland and France could not be tolerated in the gas industry.

The subsequent times imposed by Ofgem and the limited compensation paid to domestic consumers was of no help to I&C consumers whose businesses were threatened. This must not be allowed to happen in the Gas Industry, hence my argument that Ofgem take action before the event.

Moving on to the proposed Agency, I am happy that the principle can be made to work. I do still have concerns that the proposed governance arrangements, which effectively gives NGT the veto to change, could stifle innovation.

I realise that the following concern is not a DN sale issue but I was disappointed that your document did not contain the information that the IGTs had voluntarily agreed to join the Agency. I note that IDNs cannot opt out of the Agency and would welcome the news that the same applied to IGTs. Perhaps we can look forward to Ofgem pursuing the issue separately with some urgency?

The principle of comparative regulation is sound, however I note that at the same time as selling DNs Transco are centralising the remaining four. I cannot help speculating on the effect that this will have on Ofgem's ability to compare and whether if Transco had decided to centralise all eight would consumers have seen an even better outcome?

Moving on to my specific concerns, which centre around the proposed off-take arrangements. I would have preferred to begin with the original Transco proposals than with the far more complex arrangements proposed by Ofgem.

I believe that we could have begun with simple arrangements with the industry being allowed to develop change as and when necessary.

The consumers aversion to complex arrangements is affected by our experience with entry capacity auctions where we are still seeing Code mods some 5 years after the introduction of auctions. We have also experienced considerable increases in the NBP price of gas and instability of Transco's prices, both caused by auctions.

As to the proposed off-take arrangements it would appear that Ofgem have used this opportunity to dust down and re-introduce consultation 17/01 which was heavily defeated in 2001. I stated consumers' opposition at that time and will repeat them for the record.

To begin with line-pack, consumers believe that this is an element of security of supply and should remain totally in the control of the system balancer. To allow any part of this to be exposed to the vagaries of commercial decisions we believe to be wrong. Therefore I am opposed to the proposals on line pack.

With regard to within day profiling I am happy if this is purely an aid to system planning and design. If however financial penalties are attached to variations from the profile we are in effect introducing hourly balancing, to which I am totally opposed.

On the proposals for NTs exit capacity booking I have two major concerns. The first is the proposal to introduce a day ahead interruptible product. This could encourage existing firm sites, in areas where they know there are no capacity constraints, to use this facility to avoid paying for their capacity, thereby encouraging freeloading. As the NTs has a fixed revenue any under-recovery must be passed on to those booking firm capacity i.e. the DNs and effectively the LDZ consumer.

My second concern on exit capacity booking is the proposal to introduce incentives for the DN. If the incentive were to encourage the DN to under-book capacity my concern is that this will not show as a problem until we have a severe winter, thereby increasing the possibility of an emergency being declared.

Moving on to the financial aspect of the Impact Analysis. Please forgive me for not getting over excited at the prospect of £225 million spread over the 15 years 2008-2023 (a saving of about 0.04p/therm) especially as Transco have just announced a probable increase of £50 million from April '05. I also cannot help comparing it with the immediate gain to be paid to NGT's shareholders.

As the basis of the Impact Analysis is a comparison between the sale and no sale options, I believe I am safe in assuming that the £225 million benefit is in addition to the £300 million promised under the change to individual pricing of Transco's LDZs.

I note that there is a potential up front cost of £25 million associated with Shippers system development costs. I accept that Ofgem have taken a conservative approach to this area and that

the actual cost may be much less. However, whatever the figure under present arrangements it will be borne by today's consumer over the next couple of years. This I believe to be unacceptable as the cost is caused solely by NGT's decision to sell their DNs. Therefore I believe it should be NGT's shareholders who should bear all identifiable industry costs associated with the sale of DNs.

I hope I have made my views clear but will be happy to provide any further information you may require.

Yours truly,



Eddie Proffitt
Gas Group Chairman
meuc