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HEALTH AND SAFETY COMMISSION

TRANSCO - PROJECT BLACKWATER

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Issue

1. To inform the Commission of proposals being developed by National Grid Transco to sell part of Transco's gas distribution business.

Timing

2. National Grid Transco issued a brief public statement with its preliminary results on 21 May 2003.

Recommendation

3. That the Commission notes:
 - National Grid Transco's plans for the sale of part of its gas distribution business
 - The main safety-related issues identified by HSE
 - Ofgem's intention to publish a Consultative Document in collaboration with HSE on all the regulatory issues arising, in June 2003.

Background

4. Following last year's merger between National Grid and the Lattice Group (which included Transco plc), the new entity National Grid Transco has been considering proposals for a restructuring of its gas distribution business, potentially involving the sale to independent operators of a number of its eight regional Distribution Networks (DNs). We understand that the detail of the proposals, including timetable, is subject to further discussion by National Grid Transco's Board. Transco's regional DNs already operate as semi-autonomous units within the National Grid Transco group.
5. Transco will continue to own and operate the high-pressure national transmission system (NTS), and says that for the foreseeable future it intends to remain a major player in regional gas distribution.

6. The project cannot go ahead without the assent of Ofgem, exercising its powers as the licensing authority. It will also require acceptance by HSE of revisions to Transco's gas conveyor and network emergency co-ordinator safety cases, under the Gas Safety (Management) Regulations 1996, and other independent conveyor safety cases that may be affected by the restructuring, as well as new safety cases from any buyers of the DNs. Further information on Project Blackwater, relevant regulatory controls and the major issues arising is set out in the HSE framework document at **ANNEX A**.

Argument

7. Implementation of Project Blackwater would entail a major restructuring of the gas distribution industry. Transco plc is at present a highly integrated, national utility. Its role has been of critical importance in ensuring security of supply and in dealing with other safety-related issues. There is a major potential problem - for the industry, the regulatory authorities and the public - if the proposed restructuring is not handled properly.
8. HSE has identified the following areas where there are safety-related issues to be addressed:
 - Security of supply (this is also an issue for Ofgem and DTI)
 - Emergency service provision (Transco is currently the sole provider, but does not at present envisage continuing to provide this service to any independent DNs)
 - Mains replacement, in particular the accelerated programme for the replacement of iron mains that HSE agreed with the unified Transco in 2001
 - Culture change in the DNs (depends to some extent on the identity and background of any buyers of the DNs).
9. HSE is starting from the position that the future arrangements should be at least as safe as the current arrangements, in line with Fundamental Principles set out in the Commission's 1995 report on the safety implications of gas market liberalisation, Britain's Gas Supply: A Safety Framework.
10. In view of the potential risks and the work needed by all parties - including the industry and the regulatory authorities - to address them, HSE considers that the project cannot be pushed through in haste and that the timetable for any changes must allow for a full consideration of all the regulatory issues arising. Early consultation with Ofgem suggests that they share this view. Ofgem intends to publish a Consultative Document, with input from HSE, on all the regulatory issues arising. This is likely to include an Ofgem view as to the timescale needed for delivery of the project (possibly a minimum of 18 months).

Consultation

11. Internally between HSE's Hazardous Installations Division (HID), the Policy Group and HSE Press Office, and externally between HSE, Ofgem, DTI and National Grid Transco. There will also be an Ofgem-led public consultation commencing in June 2003 (paragraphs 10 and 12 refer).

Presentation

12. Ofgem, with input from HSE on safety aspects, intends to publish a Consultative Document covering all the regulatory issues towards the end of June 2003. There is likely to be a three-month public consultation period, with a review of the outcome in the autumn of 2003. HSE has briefed DWP Minister, Nick Brown, and DTI are briefing the Energy Minister.

Lines to take (if needed)

13. The following points can be made:

- we are aware of Transco's proposals
- HSE will be considering fully the safety implications
- the aim of the Commission and HSE will be to ensure that existing levels of safety are not compromised
- both HSE and Ofgem will need to give their assent to any changes in due course.

Costs and Benefits

14. The disposal of part of Transco's gas distribution business raises complex issues for the regulatory authorities. The driver is National Grid Transco's business strategy, and it is not clear that there would be any benefits for other stakeholders, unless under the future structure synergies and cost savings were achieved permitting energy price reductions to consumers. But at the present stage this remains highly speculative. HSE is determined that any such benefits are not achieved at the expense of safety. We expect that an analysis of costs and benefits will be included in the Ofgem CD.

Financial/Resource Implications for HSE

15. At this early stage, it is difficult to estimate the level and timing of the resource input required. HID is developing a project plan. It is, however, already clear that a significant resource input will be required from HID. There are also resource implications for Policy Group. Additional input may be required from other Divisions/Directorates, including FOD and Solicitor's Office.
16. Costs arising from HID's assessment of the safety cases submitted by operators of the Distribution Networks, and revisions to existing safety cases, will be recoverable under the charging regime.
17. HID envisage the need for support from external consultants, to advise on the likely impact of structural change in the industry, at an estimated cost of £30k.
18. Overall, HSE will have to re-organise and re-prioritise some of its work to ensure that there is sufficient resource and expertise available to enable the extra work arising from this project to be carried out.

Environmental Implications

19. None.

Action

20. The Commission is invited to note:

- Transco's plans for a restructuring of Britain's gas distribution system
- Safety-related issues arising from this project
- Ofgem's intention to publish in June 2003 a Consultative Document, which will include input from HSE, on the regulatory issues arising from Project Blackwater, for public comment.