

Scotia Gas Networks Limited

Report of the Compliance Officer

For the year ended 31 March 2024



Contents

	Page
Introduction	2
Overall approach	3
Managerial and operational independence	4
Common services	5
Systems and confidential information	5
Branding	6
Responsibility and monitoring	6
Complaints	7
Advisory role	7
Appendix – Duties of the Compliance Officer	



Introduction

Standard Special Condition A33 of the Gas Transporters Licences for Scotland Gas Networks plc and Southern Gas Networks plc requires that gas transportation is managed to ensure it does not restrict, prevent or distort competition elsewhere in the energy industry and that there is absolute confidentiality of related, commercially sensitive information.

Scotia Gas Networks Limited (“SGN”) owns Scotland Gas Networks plc and Southern Gas Networks plc and has published in its Statement of Compliance (last revised April 2023) how it complies with the licence requirements, specifically the full managerial and operational independence of the transportation businesses.

Standard Special Condition A34 of the Gas Transporters Licence requires SGN to appoint a Compliance Officer to facilitate compliance with the licence restrictions on the use of certain information and the independence of the transportation businesses.

Henderson Loggie LLP, Chartered Accountants, have been appointed as Compliance Officer by SGN. On behalf of Henderson Loggie LLP, the Compliance Officer role is led by Gavin Black (Partner). The licences require us to report annually to the Directors on our activities over each year to 31 March, and the licensee to report thereafter to Ofgem on the Compliance Officer’s activities and other relevant issues.

The specific duties of the Compliance Officer are included in the appendix to this report but principally we are responsible for supporting SGN with its compliance with the relevant licence conditions. This includes providing advice to SGN on complying with the confidentiality and separation obligations placed on the transportation businesses, monitoring the effectiveness of the practices, procedures and systems adopted by SGN, investigating complaints and reporting annually to the SGN Audit Committee. We are also required to liaise with Ofgem on these matters as appropriate.

This report sets out the results of our assessment of SGN’s compliance with the terms of its Statement of Compliance and hence the relevant licence conditions.



Overall approach

We have developed a Compliance Review Programme (“CRP”) which sets out the monitoring and testing we consider necessary to ensure practices, procedures, systems and controls are dealing effectively with the licence requirements on the restriction on use of certain information and independence of the transportation businesses (“Compliance”). The CRP is designed to recognise the business and legislative environment SGN operates in with regard to achieving managerial and operational independence and the approach and philosophy adopted by SGN to comply with the licence conditions.

In previous years, we have considered the formalisation and communication of Compliance procedures throughout SGN and assessed how embedded the Compliance philosophy is in the organisation. We now monitor the systems and procedures established, including any changes in this area, to obtain comfort over their ongoing effective operation.

Our main contacts at SGN include the Group Head of Audit, Risk & Compliance and the Principal Compliance Officer. We discussed with key personnel their role, issues relevant to the licence conditions and gathered evidence relevant to our monitoring role. These discussions covered legal and compliance, regulation, finance, commercial activities, HR and internal audit, and were held with a range of corporate staff. Consideration was also given to any possible Compliance issues arising out of the progression of significant commercial business activity during the year, mainly SGN Futures and SGN Commercial Services, as well as increasing commercial developments and opportunities generally.

Wherever appropriate we use SGN departments, including Internal Audit, Legal & Compliance and Regulation, to assist with our testing, with our role being to understand their risk assessment processes, review the scope of their work, the results and conclusions reached, and any remedial action taken. All other monitoring and testing is undertaken directly by ourselves and in particular has involved meeting with key individuals to discuss relevant issues and investigating critical areas such as governance, managerial separation, physical separation, IT and data confidentiality, the interaction and contracts with SSE plc (“SSE”), cross-subsidies, staff induction, training and branding.

One area of specific consideration over the years has been the relationship with and services provided by SSE and the resultant implications for SGN’s compliance with the licence conditions. SSE previously owned 33.3% of SGN and historically provided a range of corporate and commercial services, although the extent of these was reducing consistently over time. When SSE sold its equity stake in SGN in March 2022, the pre-existing MSA was replaced by a Transitional Services Agreement (TSA) covering the services that would continue to be provided by SSE in the short term. All remaining services were fully transferred during the year and the TSA ended in March 2024. The only remaining link of note between SGN and SSE is in respect of shared depots. Formal lease agreements are in place for these sites and each party is therefore treated like any other third party.

There is a clear philosophy that access to information and data should be prevented where confidentiality requires it, specifically between the regulated and unregulated areas of SGN’s business. Relevant SGN members of staff are aware of this and where commercially sensitive information which is recognised as a genuine risk to competition is involved, appropriate procedures and systems have been designed and implemented to restrict access to it. SGN places particular emphasis on confidentiality clauses in staff contracts to reinforce the importance of confidentiality and to clearly set out the disciplinary process which would follow any breach.

On 11 March 2024, SGN announced to the stock exchange that it had received notification from Ofgem of an investigation being opened under s.25 of the Competition Act 1998, focussed on the conduct of SGN and its connections business. Whilst we are aware of the investigation, due to the early stage of the process and legal restrictions on SGN providing the Compliance Officer with sufficient information, it is not yet possible to assess the impact of this investigation on SGN’s compliance with its Statement of Compliance and Standard Special Condition A33. As such, our work for 2023/24 has required to be carried out without further regard for the investigation.

Since our appointment, we have not been required to meet with Ofgem.



Managerial and operational independence

We consider there are several distinct facets which are important to achieving ongoing managerial and operational independence as required by the licence and Ofgem. In particular, as SGN does not have a gas supply business, the key aspects historically have been in relation to its managerial and operational independence from SSE's supply and gas related businesses. This has included legal and physical separation, establishment of autonomous boards and decision-making processes, establishment of contractual service level agreements, data confidentiality and branding of the separated businesses.

As noted previously, the divestment by SSE of its equity stake in SGN in March 2022 has now removed this potential area of concern going forward. However, business areas within SGN such as metering and connections, together with the level of unregulated commercial business opportunities, add to the inherent risks for Compliance and reinforce the need for appropriate service level agreements (SLAs) and treasury management within SGN, and a strong awareness across the group of confidentiality and competition law.

There is clear separation between the regulated business (including the two UK gas transportation licence holders) and the unregulated business, which includes commercial service offerings and a property sub-group. Governance is under continual review as the business changes and develops to ensure there is managerial separation between the regulated and unregulated business at Committee level, with appropriate reporting lines to the Group Executive Committee and the main Board of Directors.

The practical aspects such as the creation of separate legal entities with the appropriate split of directors and responsibilities, physical access restrictions and branding have been specifically reviewed to ensure the regulated business is independent as defined by the licence conditions. The fact that the Board is made up of representatives from each of the three shareholder groups as well as two sufficiently independent directors creates a strong framework for independent operation.

We monitor the effectiveness of strategic data confidentiality, autonomy of decision making and governance issues. This involves reviewing relevant board and audit committee minutes and discussing the managerial and strategic independence of SGN with directors and officers. It is clear from our work that SGN is run autonomously with commercial confidentiality. We have discussed the operation of the SSE TSA with management and are aware of the level of scrutiny of these arrangements applied by the Board. In recent years there had been a gradual reduction in reliance on services provided by SSE and this has now come to a natural end following SSE's divestment.

In terms of physical separation, we have confirmed over our years as Compliance Officer that physical access and security is in line with the Statement of Compliance, and that continual changes are being made to maintain this as the business grows and diversifies into more commercial activities. Any new or remodelled office premises are designed with business separation being front of mind. Where SGN operates out of shared depots with SSE, there has always been clear physical separation controlled by PAC access. Following SSE's divestment, formal leases are now in place for all shared sites, with dedicated office space and access controls.

Legal and Regulatory compliance is a specific risk recognised in the Enterprise Risk Register overseen by the Board. In addition, a formal business separation procedure is in place, owned by the Legal & Compliance Team, to reinforce SGN's commitment to business separation. These, together with the operation of the Business Separation Working Group, provide a strong framework which runs through to the Board.

The ongoing reinforcement of confidentiality and training amongst staff, the importance attached to it by senior management and the seriousness with which SGN would regard any breaches continues to ensure the underlying philosophy and approach adopted by SGN in this area is maintained.



Common services

SSE has a gas supply business and an involvement in gas transportation and up until its divestment, we had considered the implications of SSE owning 33.3% of SGN in terms of SGN's operation and management. As SGN does not have its own gas supply business, this risk is now significantly reduced.

We have also considered other aspects such as physical access to premises, systems access and staff transfers and are satisfied that no separation issues have arisen. In addition, the audit of the regulatory accounts includes specific agreed upon procedures reporting by the auditors on cross subsidies and no areas of concern have been identified. Furthermore, Internal Audit carried out a specific review of Financial Separation during the year, with no major findings being reported.

An intercompany Master Services Agreement (MSA) is in place to provide an overarching governance framework for intra-group services provided within the SGN corporate group, with supporting schedules for each specific service including provisions around pricing and service levels.

As previously noted, we are unable at this stage to assess any impact of the Competition Act investigation on compliance in this area. However, aside from this, there have been no external complaints regarding common services or cross subsidies which suggests that the practices adopted are not anti-competitive. As a result, SGN's procedures and controls appear to be appropriate to guard against access to or use of confidential information, to prevent any anti-competitive practices and to preserve the independence of the transportation businesses.

Systems and confidential information

Internal Audit has previously reviewed this area from a Compliance perspective and their work confirmed that access controls for finance and other key systems were operating as designed providing assurance that the licence conditions were being complied with. Access to finance systems was reviewed again as part of the Internal Audit of Financial Separation during the year.

System controls, physical access controls and whilst it was relevant, the terms of the TSA with SSE, provide a robust environment to control access to and the use of confidential information. Where SGN operates out of shared depots with SSE, there has always been clear physical separation controlled by PAC access. Following SSE's divestment, formal leases are now in place for all shared sites, with dedicated office space and access controls.

"Two-Hats" guidance is in place to give further support to SGN corporate staff who provide services to both the regulated and unregulated businesses. This helps identify which role these individuals are fulfilling at any point in time and how to manage confidential information when working with other parties, and also ensuring it is not used by these individuals in fulfilling their other roles.

SGN employment contracts and letters of appointment specifically address confidentiality and the disciplinary procedures that would apply to breaches in this area. A formal induction package is in place and a Compliance Communications Strategy has been developed to cascade key board messages and directives including confidentiality, data protection, business separation and whistleblowing to ensure all staff are aware of the key requirements.

SGN has identified that staff transferring between the regulated and unregulated businesses could have regulatory implications. Accordingly, HR and Compliance have established formal procedures to assess all staff transfers to identify any such issues so that appropriate steps can be taken if potential business separation issues exist.

SGN has created a strong corporate identity and compliance culture, and this is reinforced further through specific training on business separation which is rolled out across the entire business. The depth of the training is tailored to the role and related business separation risk as set out in the Compliance Training Strategy. Training has been provided to almost 4,200 employees during 2023/24



through a mix of eLearning and videos, depending on the extent of business separation risk attaching to individual roles. Face to face training for those individuals in higher risk roles was planned for the second half of 2023/24, however this was postponed to the first half of 2024/25 due to other key business priorities. This training needs to be provided as soon as possible in order to bring training back in line with the Compliance Training Strategy.

Branding

The effectiveness of branding is an important aspect of SGN's stated policy and is reinforced in the marketplace through vehicles, staff, PPE and publications. Separate brand identities have been developed for unregulated businesses and we are satisfied that branding is in keeping with the SGN policy and is consistent with the requirements of the licence conditions.

Responsibility and monitoring

The importance of Compliance as a key risk within the organisation is clearly recognised by the Board and Audit Committee and is included on the Enterprise Risk Register. Systems, policies and procedures reinforce this and demonstrate group wide awareness.

Whilst ultimate responsibility rests with the Board, it is a key requirement for executives and managers to ensure compliance with the SGN's business separation and related procedures and the relevant Licence conditions within their own business areas. Internal monitoring of Compliance is carried out by the Legal & Compliance team, supported by Regulation.

A significant amount of work has been undertaken in recent years following an all-encompassing review and refresh of business separation processes and procedures. This project has resulted in improved training materials and a suite of policies and procedures on Compliance training and communications, management of confidential information and "Two-Hats" guidance for corporate staff who provide services across the regulated and unregulated businesses.

The Business Separation Working Group guides and monitors SGN's annual compliance plan and directs SGN's approach to business separation requirements. Membership of this group includes senior personnel from areas including Legal and Compliance, Regulation, Finance, HR, IT, Property and Operations (regulated and unregulated) to ensure that all key aspects of business separation are considered. Clear terms of reference are in place to define the purpose and measure the performance of this group. The Ethics and Compliance Committee also supports the overall compliance framework and culture of SGN, albeit it does not have a specific remit with regard to business separation.

As an independent external Compliance Officer, our approach brings an objective review of the practices and procedures in place or planned to help ensure the conditions of the licence and the Statement of Compliance are being met.



Complaints

We have agreed a procedure whereby any complaints received relating to business separation in connection with the regulated business will be immediately forwarded to us setting out the investigation work to be undertaken by SGN. Thereafter we will receive details of SGN's response to the complainant and any remedial action taken or proposed. We would then decide whether it is necessary to undertake our own investigation. Whilst there can be no guarantee that every relevant complaint would be dealt with by the Legal & Compliance Team, we are satisfied that all those with substance would be notified to Legal & Compliance and thereafter the above procedure would be applied.

Aside from the Competition Act investigation, we have not been advised of any business separation or Compliance complaints during the year under review.

Advisory role

Our remit as Compliance Officer includes providing input on business separation issues to help ensure policies and procedures are consistent with the Statement of Compliance and meet the expectations of Ofgem where practicable.

Regular contact with the Legal & Compliance team allows such issues to be aired and addressed as they arise.

SGN systems and procedures are well established and are operating effectively. Accordingly, our ongoing role will be to continue to monitor the effectiveness of the Compliance systems and procedures established throughout the organisation.

Where appropriate, we will continue to provide assistance and an independent external view on Compliance matters and the development of the management and operational systems, procedures and controls. We will also work with the business in due course to provide any required input on the Competition Act investigation once details of this can be disclosed to us.



Gavin Black
Partner
For and on behalf of Henderson Loggie LLP
Chartered Accountants
Dundee Office

23 July 2024

Appendix – Duties of the Compliance Officer

- 1.1 The duties and tasks assigned to the Compliance Officer shall include:
- a) providing relevant advice and information to the licensee for the purpose of ensuring its compliance with the relevant duties;
 - b) monitoring the effectiveness of the practices, procedures and systems adopted by the Licensee in accordance with the statement referred to at paragraph 4 of Standard Special Condition A33 (Restriction on use of Certain Information and Independence of the Transportation Business);
 - c) advising whether, to the extent that the implementation of such practices, procedures and systems requires the co-operation of any other person, they are designed so as reasonably to admit the required co-operation;
 - d) investigating any complaint or representation made available to him in accordance with paragraph 4;
 - e) recommending and advising upon the remedial action which any such investigation has demonstrated to be necessary or desirable;
 - f) providing relevant advice and information to the licensee for the purpose of ensuring its effective implementation of:
 - i) the practices, procedures and systems adopted in accordance with the statement referred to above; and
 - ii) any remedial action recommended in accordance with sub-paragraph (e); and
 - g) reporting annually to the directors of the licensee – in respect of the year ending 31 March 2007 and of each subsequent year – as to his activities during the period covered by the report, including the fulfilment of the other duties and tasks assigned to him by the licensee.
- 1.2 As soon as is reasonably practicable following each annual report of the Compliance Officer, the Licensee shall produce a report:
- a) as to its compliance during the relevant year with the relevant duties; and
 - b) as to its implementation of the practices, procedures and systems adopted in accordance with the statement referred to above.



- 1.3 The report produced in accordance with paragraph 1.2 above shall in particular:
- a) detail the activities of the Compliance Officer during the relevant year;
 - b) refer to such other matters as are or may be appropriate in relation to the implementation of the practices, procedures and systems adopted in accordance with the statement referred to above; and
 - c) set out the details of any investigations conducted by the Compliance Officer, including:
 - i) the number, type and source of the complaints or representations on which such investigations were based;
 - ii) the outcome of such investigations; and
 - iii) any remedial action taken by the Licensee following such investigations.



Aberdeen 45 Queen's Road AB15 4ZN

Dundee The Vision Building, 20 Greenmarket DD1 4QB

Edinburgh Ground Floor, 11-15 Thistle Street EH2 1DF

Glasgow 100 West George Street, G2 1PP

T: 01224 322 100

T: 01382 200 055

T: 0131 226 0200

T: 0141 471 9870

F: 01224 327 911

F: 01382 221 240

F: 0131 220 3269

Henderson Loggie LLP is a limited liability partnership registered in Scotland with registered number SO301630 and is a member of PrimeGlobal, a global association of independent accounting firms, the members of which are separate and independent legal entities. Registered office is: The Vision Building, 20 Greenmarket, Dundee, DD1 4QB. All correspondence signed by an individual is signed for and on behalf of Henderson Loggie LLP. Reference to a 'partner' is to a member of Henderson Loggie LLP. A list of members' names is available for inspection at each of these addresses.

