

**Modification Report**  
**Provision of Cost Information**  
**Modification Reference Number 0186/0186A**  
**Version 5.0**

This Modification Report is made pursuant to Rule 9.3.1 of the Modification Rules and follows the format required under Rule 9.4.

**1 The Modification Proposal**

Proposal 0186

This Proposal seeks to extend the scope of Modification Proposal 698 to provide the detailed information Shippers require about the core elements of Gas Distribution price control as detailed below. This will enable them to forecast more accurately the likely direction and magnitude of changes in transportation revenue over the remaining period of the current Gas Distribution price control, and over the forthcoming years of the next price control. It is the intention of this modification that information provided by the DNs will be used by shippers for their own forecasting purposes and that DNs will not be held accountable for errors or omissions. It is expected however that the DNs will endeavour to provide their best view at all times. Furthermore, it is not the intention of this modification that information provided by the DNs will be challenged by the shippers, although reasonable questioning can be expected.

Table of required information

Revenue element	Annual target (projected forward for 5 years)*	Quarterly reforecast of annual outturn (difference)
Core allowed (Z) <sup>\$</sup>		Not applicable
Cost pass through (F) <sup>\$</sup>		
Incentive payments and adjustments, shrinkage, exit cap, IAE, MRA etc. <sup>\$</sup>		
Inflation rate assumed		Update with latest RPI data
Over/under recovery (K) <sup>\$</sup>	Not applicable	
Supplemental information derived from the above		

Final allowed revenue (MOD)	Not applicable	
Final allowed revenue forecast (MOD)	Not applicable	
Forecast collected revenue	Not applicable	
Arithmetical Price change required at next Charging year	Not applicable	
Commentary, definitions and assumptions <sup>#</sup>	To assist in the understanding of the data presented	To assist in the understanding of the data presented

An example spreadsheet in Excel format is attached to clarify the precise format of this report

\* It is recognized that the relevant price control ends after five years and there is uncertainty over forecasts beyond that horizon. Any forecasts beyond the relevant price control will be based on assumptions as agreed by both the DNs and Shippers which will take into account any relevant Ofgem publications and latest Price Control proposals.

\$ The terms Z, F and K have the meaning attributed to them in the relevant Price Control review. The 'incentives payment and adjustments' is an aggregate of all incentives and the mains replacement adjustment.

# The UNC will be changed to reflect the requirement for a commentary, definitions and assumptions.

It is envisaged that this information will be posted onto the relevant DN websites, but preferably all together on the Joint Office website. A quarterly meeting will be arranged to present this information to interested shippers, as well as other relevant topics, for example the Distribution Charges Methodology Forum (DCMF).

Timetable:

The quarterly actual and updated target information should be made available on the 10<sup>th</sup> working day of the second calendar month after the end of the month to be reported. Example dates for 2008 are shown below:

15 <sup>th</sup> January 2008	for data up to the end of November 2007
14 <sup>th</sup> April 2008	for data up to the end of February 2008
14 <sup>th</sup> July 2008	for data up to the end of May 2008
14 <sup>th</sup> October 2008	for data up to the end of August 2008

or the nearest convenient regular meeting schedule, e.g. the 2<sup>nd</sup> Monday of each quarter month.

With greater transparency of the elements that make up the Price controlled revenue, Shippers and their related Suppliers can better assess the impact of revenue changes upon their business and the pricing of services to their customers. Shippers are currently unable to forecast future revenues with any certainty and cannot accurately assess future changes to transportation charges.

This information has become significantly more important now that there are effectively eight separate price controls for each GDN. The latest indicative charges show an average 26.5% increase in charges versus an inflation figure of 4.5%. These changes also show a wide variation from 2.9% to 64.0% between the different GDNs. Much more detailed information is required to enable Shippers to forecast such large and diverse changes to their costs and consequently provide better informed customer pricing decisions.

Once the new reporting is in place and seen to be working satisfactorily by the shippers, a further Proposal may be raised in order to stop the Modification 698 process.

#### Proposal 0186A

This Proposal seeks to extend the scope of Modification Proposal 698 to provide the detailed information Shippers require about the core elements of Gas Distribution price control as detailed below. This may help them to forecast the likely direction and magnitude of changes in transportation revenue over the remaining period of the current Gas Distribution price control. It is the intention of this modification that information provided by the DNs will be used by shippers for their own forecasting purposes and that DNs will not be held accountable for errors or omissions. It is expected however that the DNs will endeavour to provide their best view at all times. Furthermore, it is not the intention of this modification that information provided by the DNs will be challenged by the shippers, although reasonable questioning can be expected.

Table of required information

Revenue element	Annual target (projected forward to the end of the price control period)*	Quarterly reforecast of annual outturn (difference)
Core allowed (Z) <sup>\$</sup>		Not applicable
Cost pass through (F) <sup>\$</sup>		
Incentive payments and adjustments, shrinkage, exit cap, IAE, MRA		

etc. <sup>\$</sup>		
Inflation rate assumed		Update with latest RPI data
Over/under recovery (K) <sup>\$</sup>	Not applicable	
Supplemental information derived from the above		
Final allowed revenue (MOD)	Not applicable	
Final allowed revenue forecast (MOD)	Not applicable	
Forecast collected revenue	Not applicable	
Arithmetical Price change required at next Charging year	Not applicable	
Commentary, definitions and assumptions <sup>#</sup>	To assist in the understanding of the data presented	To assist in the understanding of the data presented

An example spreadsheet in Excel format is attached to clarify the precise format of this report

\* Each price control period normally lasts for five years and it is not possible to forecast beyond the end of the existing price control period. Any projections beyond the existing price control could be misleading and not in keeping with the purpose of this Modification proposal. DNs will however discuss possible outcomes of the next price control period with Shippers at the DCMF. Once Ofgem has published specific proposals for the following price control period the DNs will start publication in a Mod186A format for that price control period.

<sup>\$</sup> The terms Z, F and K have the meaning attributed to them in the relevant Price Control review. The 'incentives payment and adjustments' is an aggregate of all incentives and the mains replacement adjustment.

<sup>#</sup> The UNC will be changed to reflect the requirement for a commentary, definitions and assumptions.

This information will be posted on the Joint Office website. A quarterly meeting will be arranged to present this information to interested shippers, as well as other relevant topics, for example the Distribution Charges Methodology Forum (DCMF).

Timetable: The quarterly actual and updated target information should be made available on the 10<sup>th</sup> working day of the second calendar month after the end of the month to be reported. Example dates for 2008 are shown below:

15<sup>th</sup> January 2008 for data up to the end of November 2007  
14<sup>th</sup> April 2008 for data up to the end of February 2008  
14<sup>th</sup> July 2008 for data up to the end of May 2008  
14<sup>th</sup> October 2008 for data up to the end of August 2008

or the nearest convenient regular meeting schedule, e.g. the 2<sup>nd</sup> Monday of each quarter month.

With greater transparency of the elements that make up the Price controlled revenue, Shippers and their related Suppliers can better assess the impact of revenue changes upon their business and the pricing of services to their customers.

This information has become significantly more important now that there are eight GDNs. The latest indicative charges show an average 26.5% increase in charges versus an inflation figure of 4.5%. These changes also show a wide variation from 2.9% to 64.0% between the different GDNs. Much more detailed information is required to enable Shippers to forecast such large and diverse changes to their costs and consequently provide better informed customer pricing decisions.

Once the new reporting is in place and seen to be working satisfactorily by the shippers, a further Proposal should be raised in order to stop the Modification 698 process.

## **2 Extent to which implementation of the proposed modification would better facilitate the relevant objectives**

*Standard Special Condition A11.1 (a): the efficient and economic operation of the pipe-line system to which this licence relates;*

The charging methodology for GDNs to recover their allowed revenue from system users is governed by obligations set out under standard condition 4A of the Transporter's GT licence. Both Proposals would allow Shippers to forecast changes to these charges, which is not possible currently.

Under standard condition 9 of their GT licence, Transporters have an obligation to establish economic transportation charging arrangements which facilitate the efficient and operation of their pipeline system, secure effective competition between relevant shippers and suppliers and which secure domestic customer security standards. Transporters are also required to ensure that their charges reflect the costs that they incur in their transportation business. In setting charges, Transporters are required to use best endeavours to set transportation charges such that the total revenue from such charges does not exceed their allowed revenue in any given year.

Scotia Gas Networks does not agree with this assertion since implementation of the Proposal would not provide any additional information to GDNs.

***Standard Special Condition A11.1 (b): so far as is consistent with subparagraph (a), the coordinated, efficient and economic operation of***

- (i) the combined pipe-line system, and/ or***
- (ii) the pipe-line system of one or more other relevant gas transporters;***

Implementation would not be expected to facilitate the achievement of this objective.

***Standard Special Condition A11.1 (c): so far as is consistent with subparagraphs (a) and (b), the efficient discharge of the licensee's obligations under this licence;***

Standard Condition 9 of the Transporters GT Licence has an obligation to establish economic charging arrangements which facilitate the efficient operation of the pipeline system, secure effective competition between relevant Shippers and which secure domestic security standards. EDF Energy believe that, since this Proposal should help to secure effective competition between Shippers, it should therefore also further this relevant objective.

***Standard Special Condition A11.1 (d): so far as is consistent with subparagraphs (a) to (c) the securing of effective competition:***

- (i) between relevant shippers;***
- (ii) between relevant suppliers; and/or***
- (iii) between DN operators (who have entered into transportation arrangements with other relevant gas transporters) and relevant shippers;***

Implementation would provide Shippers with information that could be used to more accurately forecast changes to transportation charges. By making forecasts of future charges more accurate, Shippers and Suppliers would face less uncertainty and risk. Reducing risk and uncertainty facilitates the securing of effective competition between relevant Shippers and between relevant Suppliers.

***Standard Special Condition A11.1 (e): so far as is consistent with subparagraphs (a) to (d), the provision of reasonable economic incentives for relevant suppliers to secure that the domestic customer supply security standards... are satisfied as respects the availability of gas to their domestic customers;***

Implementation would not be expected to facilitate the achievement of this objective.

***Standard Special Condition A11.1 (f): so far as is consistent with subparagraphs (a) to (e), the promotion of efficiency in the implementation and administration of the network code and/or the uniform network code;***

Implementation would not be expected to facilitate the achievement of this

objective.

**3 The implications of implementing the Modification Proposal on security of supply, operation of the Total System and industry fragmentation**

There are no implications on security of supply, operation of the Total System or industry fragmentation

**4 The implications for Transporters and each Transporter of implementing the Modification Proposal, including:**

**a) Implications for operation of the System:**

No such implications have been identified.

**b) Development and capital cost and operating cost implications:**

Some development may be required, but whilst the Proposer is unable to provide an estimate he believes that these costs should be minimal as the Proposer understands that this information is already available to Transporters.

**c) Extent to which it is appropriate to recover the costs, and proposal for the most appropriate way to recover the costs:**

No cost recovery is required

**d) Analysis of the consequences (if any) this proposal would have on price regulation:**

No such consequences have been identified.

**5 The consequence of implementing the Modification Proposal on the level of contractual risk of each Transporter under the Code as modified by the Modification Proposal**

No such consequence is anticipated.

**6 The high level indication of the areas of the UK Link System likely to be affected, together with the development implications and other implications for the UK Link Systems and related computer systems of each Transporter and Users**

Some development may be required, but the Proposer believes that that this information is already available to Transporters.

**7 The implications of implementing the Modification Proposal for Users, including administrative and operational costs and level of contractual risk**

*Administrative and operational implications (including impact upon manual processes and procedures)*

No such implications have been identified.

***Development and capital cost and operating cost implications***

No such implications have been identified.

***Consequence for the level of contractual risk of Users***

No such consequences have been identified.

**8 The implications of implementing the Modification Proposal for Terminal Operators, Consumers, Connected System Operators, Suppliers, producers and, any Non Code Party**

Large consumers tend to have supply contracts with gas transportation cost pass through, thereby exposing them to the risk that Transportation Charges will increase, or decrease in the future. EDF Energy believe both modification proposals will provide these customers with a view of likely future transportation charges that will allow them to plan their businesses more effectively. Proposal 0186 will be more beneficial as it will provide consumers with a longer horizon on which to plan their business. It should also be noted that by reducing the risk of unexpected transportation charge changes in the future, Shippers' risk premium will also be reduced which will be passed onto to consumers with fixed price contracts.

**9 Consequences on the legislative and regulatory obligations and contractual relationships of each Transporter and each User and Non Code Party of implementing the Modification Proposal**

No such implications have been identified.

**10 Analysis of any advantages or disadvantages of implementation of the Modification Proposal**

**Advantages**

- Provides additional information to the market which can help Shippers make more accurate predictions of the likely path of transportation charges.
- Increased transparency for consumers with transportation cost pass through contracts, allowing them to plan their business more effectively.
- Proposal 0186 will allow consumers and Shippers to use the transportation forecasts to plan their business up to 5 years out.

**Disadvantages**

Proposal 0186A will create a diminishing horizon of future transportation charges, as views will only be developed when Ofgem has published indicative GDPCR proposals.



**11 Summary of representations received (to the extent that the import of those representations are not reflected elsewhere in the Modification Report)**

Representations were received from the following:

	0186	0186A	Pref
British Gas Trading	Support	Not in support	0186
E.ON UK	Support	Not in support	0186
EdF Energy	Support	Support	0186
National Grid Distribution	Not in Support	Support	0186A
Northern Gas Networks	Not in Support	Qualified Support	0186A
RWE npower	Support	Not in support	0186
Scotia Gas Networks	Not in Support	Support	0186A
Wales & West Utilities	Support	Support	0186A

Thus, of the eight respondents, five supported implementation of Proposal 0186 and three did not support implementation.

In respect of Proposal 0186A, four supported implementation, one offered qualified support and three did not support implementation.

Four expressed a preference for 0186 and four expressed a preference for 0186A.

British Gas Trading and RWE believed that Users should have the opportunity to review and comment on the legal text before a decision is made on these Proposals. Northern Gas Networks gave qualified support to 0186A subject to the provision of the Legal Text and the provision of appropriate governance.

NGN did not consider it appropriate to use arbitrary assumptions to calculate Allowed Revenue beyond the end of the current price control, due to the risk that they could be incorrectly interpreted. However RWE believed that Shippers will be fully aware that projections into the next Price Control will be on the basis of agreed assumptions and treat them accordingly.

National Grid Distribution also believed it would not be appropriate to provide forecasts based upon a high level of uncertainty and acknowledged the risk that some Users will make decisions based upon the information provided. They believed the accuracy of long term forecasts and impact on User decisions could detrimentally impact upon the DNOs reputation and relationship with such Users.

**12 The extent to which the implementation is required to enable each Transporter to facilitate compliance with safety or other legislation**

Implementation is not required to enable each Transporter to facilitate compliance with safety or other legislation

**13 The extent to which the implementation is required having regard to any proposed change in the methodology established under paragraph 5 of Condition A4 or the statement furnished by each Transporter under paragraph 1 of Condition 4 of the Transporter's Licence**

Implementation is not required having regard to any proposed change in the methodology established under paragraph 5 of Condition A4 or the statement furnished by each Transporter under paragraph 1 of Condition 4 of the Transporter's Licence.

**14 Programme for works required as a consequence of implementing the Modification Proposal**

No programme of works has been identified.

**15 Proposed implementation timetable (including timetable for any necessary information systems changes and detailing any potentially retrospective impacts)**

As soon as possible

**16 Implications of implementing this Modification Proposal upon existing Code Standards of Service**

No implications of implementing this Modification Proposal upon existing Code Standards of Service have been identified.

**17 Recommendation regarding implementation of this Modification Proposal and the number of votes of the Modification Panel**

At the Modification Panel meeting held on 21 February 2008, of the 10 Voting Members present, capable of casting 10 votes, 6 votes were cast in favour of implementing Modification Proposal 0186. Therefore the Panel recommended implementation of Modification Proposal 0186. At the same meeting, 7 votes were cast in favour of implementing Alternative Proposal 0186A. Therefore the Panel recommended implementation of Alternative Proposal 0186A.

The Panel then proceeded to vote on which of the two Proposals would be expected to better facilitate achievement of the Relevant Objectives. Of the 10 Voting Members present, capable of casting 10 votes, 4 votes were cast in favour of implementing Proposal 0186 in preference to Alternative Proposal 0186A, and 4 votes were cast in favour of implementing the Alternative Proposal 0186A in preference to Proposal 0186.

**18 Transporter's Proposal**

This Modification Report contains the Transporter's proposal to modify the Code and the Transporter now seeks direction] from the Gas and Electricity Markets Authority in accordance with this report.

**19 Text**

**Proposal 0186**

**SECTION V – GENERAL**

Amend references in paragraph 5.12 of "Transporter" to NTS Operator

Insert new paragraph 5.13 & renumber existing paragraph 5.13 as 5.14.

### **5.13 DN OPERATOR COST INFORMATION**

"5.13.1 For the purposes of this paragraph 5.13 and Annex V4.

- a) **"Quarter"** shall mean a three month period ending on November, February, May and August (inclusive) in any year;
- b) **"Forecast Collected Revenue"** shall mean the DN Operator's reasonable estimate of the revenue to be recovered in respect of the relevant Formula Year referred to using such criteria as the DN Operator shall consider reasonably appropriate and having regard to the provisions of the DN Operator's Transportation Statement and any revenue or price control restrictions to which it may be subject from time to time (it being acknowledged that such estimate may be subject to revision from time to time);
- c) **"Final Allowed Revenue"** shall mean an amount reasonably determined by the DN Operator on an accruals basis (based on such information as is reasonably available to it at the relevant time) of revenue recovered or to be recovered in respect of a relevant Formula Year (it being acknowledged that such amount may be subject to a re-determination from time to time);
- d) The terms **"Z, F and K"** shall have the meanings attributed to them in the relevant DN Operator's Gas Transporters' Licence in respect of the relevant Formula Year;
- e) references to incentives, payments and adjustments are to be construed in aggregate in the context of a Distribution Network;
- f) **"Cost Information"** shall mean the information in respect of the relevant Formula Year set out in Annex V4 in the format prescribed from time to time, including any commentary as appropriate;
- g) **"Required Date"** shall mean the 10<sup>th</sup> Business Day of the second calendar month following the end of the Quarter for which the information prescribed in Annex V4 is being provided.

5.13.2 A DN Operator shall arrange for the publication each Quarter of the Cost Information by the Required Date on the website of the Joint Office of Gas Transporters.

5.13.3 Cost Information beyond the expiry of the DN Operator price control period ending 31 March 2013 will be based on assumptions to be subject to further agreement between the DN Operators and Shippers."

Amend references within Annex V3 of "Transporter" to " NTS Operator"

Insert Annex V.4.

Table of required information

Revenue element	Annual target (projected forward for 5 years)*	Quarterly reforecast of annual outturn (difference)
Core allowed (Z) <sup>\$</sup>		Not applicable
Cost pass through (F) <sup>\$</sup>		
Incentive payments and adjustments, shrinkage, exit cap, IAE, MRA etc. <sup>\$</sup>		
Inflation rate assumed		Update with latest RPI data
Over/under recovery (K) <sup>\$</sup>	Not applicable	
Supplemental information derived from the above		
Final allowed revenue (MOD)	Not applicable	
Final allowed revenue forecast (MOD)	Not applicable	
Forecast collected revenue	Not applicable	
Arithmetical Price change required at next Charging year	Not applicable	
Commentary, definitions and assumptions <sup>#</sup>	To assist in the understanding of the data presented	To assist in the understanding of the data presented

For and on behalf of the Relevant Gas Transporters:

**Tim Davis**  
**Chief Executive, Joint Office of Gas Transporters**

Joint Office of Gas Transporters  
0186/0186A: "Provision of Cost Information"

Example Spreadsheets

	20078	20089	200910	201011	201112	201213
Core Allowed	211	212	212	212	212	212
Cost Pass Through	28	28	28	28	28	28
Incentives	13	13	13	13	13	13
<b>Final Allowed Rev per PCR</b>	<b>252.0</b>	<b>253.0</b>	<b>263.2</b>	<b>266.0</b>	<b>267.3</b>	<b>262.6</b>
Inflation Assumed	1.05	1.08	1.11	1.15	1.18	1.22
<b>Final Allowed Rev per PCR at prices of year</b>	<b>264.6</b>	<b>273.6</b>	<b>293.2</b>	<b>305.2</b>	<b>315.9</b>	<b>319.6</b>
Cost Pass through Movements	1.0	0.0	0.0	0.0	0.0	0.0
Incentives Movement	1.0	0.0	0.0	0.0	0.0	0.0
K Movement	0.0	0.4	0.0	0.0	0.0	0.0
<b>Final Allowed Revenue Latest Forecast</b>	<b>266.6</b>	<b>274.0</b>	<b>293.2</b>	<b>305.2</b>	<b>315.9</b>	<b>319.6</b>
% of previous year	100.7%	102.8%	107.0%	104.1%	103.5%	101.2%
<b>Forecast Collected Revenue</b>	<b>267.0</b>	<b>274.0</b>	<b>293.2</b>	<b>305.2</b>	<b>315.9</b>	<b>319.6</b>
<b>Forecast Under / Over Recovery ( K )</b>	<b>-0.4</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>
<b>Arithmetical October Price level change needed for Collected to = Allowed</b>	<b>26%</b>	<b>-9%</b>	<b>5%</b>	<b>-2%</b>	<b>2%</b>	<b>0%</b>

Commentaries