

Mr. Julian Majdanski  
**Joint Office of Gas Transporters**  
31 Homer Road  
Solihull  
B91 3LT

Steve Armstrong  
Pricing & Margins Manager

[steve.armstrong@uk.ngrid.com](mailto:steve.armstrong@uk.ngrid.com)  
Direct tel +44 (0)1926 655834  
Direct fax +44 (0)1926 656620

[www.nationalgrid.com](http://www.nationalgrid.com)

Date: 7 February 2008  
Our Reference: 0186/0186A  
Your Reference: 0186/0186A

## **RE: Modification Proposals 0186 and 0186A – Provision of Cost Information**

Dear Julian,

Thank you for your invitation seeking representation with respect to the above Modification Proposals. National Grid Gas Distribution (National Grid) **does not support implementation of Proposal 0186** and **does support the implementation of Proposal 0186A**. National Grid welcomes Uniform Network Code (UNC) changes that would improve the existing Modification 0698 regime. However, with regard to the rolling 5 year reporting requirement, National Grid does not believe that Modification Proposal 0186 is fully developed at this time. National Grid believes that Modification Proposal 0186A addresses the limitations of 0186 and provides the information necessary to satisfy the proposal's objective.

### Overview

Network Code Modification 0698 was implemented with the intention of providing gas Distribution Network Operator (DNO) Transportation Charge (referred to as "Prices" throughout) information to enable Users to estimate the magnitude and direction of future Prices. Modification 0698 was implemented despite significant limitations. Specifically, Modification 0698 provides a monthly comparison between the DNO budget and collected revenue. This does not take into consideration, any changes to the budget over the period, does not provide a full years view of the budget until the year end, and does not show the forecasted revenue for the subsequent year. Consequently, Modification 0698 would lead to inaccurate estimates of any under or over recovery brought forward, would not enable Users to estimate the impact from allowed revenue changes between periods and ultimately lead to inaccurate estimations of future Prices. Accordingly, National Grid considers the existing UNC obligations in respect of Modification 0698 to be unfit for purpose, misleading and ineffective, and National Grid welcomes improvements as advocated by Modification Proposals 0186 and 0186A.

Modification Proposal 0186 would require the DNO to provide a projection of the DNO's allowed revenue, cost pass through and incentives as defined within the relevant network Ofgem Final Proposals. The DNO would also be required to provide an RPI adjustment factor, any forecast movements in the cost pass through and incentive values, the value of under or over recovery brought forward, the total allowed revenue and arithmetic price change required to amend the Prices (applicable at the date of reporting) to recover the allowed revenue in each year. DNOs would also be required to provide a full year projection for a rolling 5 year period to be updated quarterly.

Modification Proposal 0186A incorporates the same provisions as Proposal 0186 albeit restricting the projection to the end of the relevant Price Control Period as opposed to the rolling 5 year period proposed by Modification Proposal 0186.

### Relevant Information to Estimate Future Year Transportation Charges

Subject to any changes in the DNO Transportation Charging Methodology, the Transportation Charge movement between periods depends upon the difference between the forecast level of collected revenue from existing charges and typically the maximum allowed revenue for the period (the formula year commences 1<sup>st</sup> April to the 31<sup>st</sup> March). Accordingly, a view of the maximum allowed revenue including any under or over recovery values brought forward is required to enable an estimation of the magnitude and direction of future Prices. The maximum allowed revenue is calculated by the addition of the allowed revenue, cost pass through value, incentives and adjustments value, and any under or over recovery brought forward. Both Modification Proposals 0186 and 0186A identify the relevant information required as well as including a forecast Price change. National Grid considers this approach to be a significant improvement to the existing Modification 0698 regime.

### Rolling 5 Year Forecasts

Modification Proposal 0186 acknowledges that the 'allowed revenue' values accepted as part of a Price Control Review (PCR) are the fundamental basis for revenue and pricing forecasts. Modification Proposal 0186 would require DNOs to provide a rolling 5 year forecast hence this would require DNOs to provide a forecast for the period April 2013 to March 2014, from April 2009 and so on for subsequent years. DNOs would have limited information to derive such forecasts with the same level of accuracy as previous periods until the acceptance of the subsequent PCR.

Discussions within Review Group 0162 revealed that some Users have a preference for some form of forecast beyond the accepted PCR incorporated into the Modification Proposal.

Any forecast not based on values set out under an accepted PCR would be highly subjective and would result in a high level of uncertainty. Consequently, National Grid believes that such forecasts, those not based on accepted PCR information, would be of limited value or relevance to the community as actual price movements could be considerably different. National Grid does not believe it would be appropriate to provide forecasts based upon such a high level of uncertainty. Despite legal disclaimers and the lack of warranty concerning the accuracy and use of the information, National Grid acknowledges there is a risk that some Users will make decisions based upon the information provided. The accuracy of long term forecasts and impact on User decisions could detrimentally impact upon the DNOs reputation and relationship with such Users. Furthermore, National Grid is aware that some Users already estimate DNO Prices on a long term basis and often on a rolling basis without any assistance from the DNOs. It is highly likely that Users would wish to make different assumptions to future DNO revenue levels for those periods not included in an accepted

PCR, which brings into question the value of DNOs setting a forecast for periods beyond an accepted PCR period.

Modification Proposals 0186 and 0186A reference Ofgem's PCR Final Proposal Document as the basis for Price estimations. National Grid is concerned that no basis is defined within Modification Proposal 0186 to derive estimated Price changes beyond the PCR period. As an alternative it would require Users and DNOs to agree assumptions for forecasts beyond the accepted PCR period. However, it is unclear to us how such agreement will be brought about. Modification Proposal 0186 fails to define any process for determining what assumptions to include, how to derive such assumptions, what mechanism is to be used to formally agree assumptions and how any subsequent mechanism to amend assumptions would be managed.

National Grid understands that Review Group 0162 will continue to convene with a view to developing an additional Modification Proposal to define the governance arrangements concerning the future amendments to the Modification Proposals 0186 / 0186A reporting template and to remove DNO UNC obligations defined under Modification 0698. It is understood that any subsequent Modification would be proposed after the implementation of Proposal 0186 or 0186A so that Users are able to gain some confidence in the reporting before the proposed removal of DNO Modification 0698 provisions. Accordingly, the development of processes to define and agree assumptions for periods beyond an accepted PCR period depends upon the successful implementation of a future Modification and then the subsequent development from a governance body of those processes. It is unreasonable to place obligations and risk on a DNO when such obligations are dependant upon the outcome of further developments that are unknown at this time.

Given the level of uncertainty around the development of such processes, National Grid does not believe that a rolling 5 year period should be included within the proposal without further development. National Grid believes it is vital to have a mechanism that operates to the satisfaction of all parties as a starting point with the opportunity to further develop the reporting mechanism over time and without placing obligations that are subject to further developments. As such, National Grid believes that only Modification Proposal 0186A provides an appropriate level of information and is developed to a stage that could be implemented at this time.

Please contact Steve Marland on 01926 656912 should you require any further information.

Yours Sincerely

**Steve Armstrong**

By E-mail