

Julian Majdanski
Joint Office of Gas Transporters
31 Homer Road
Solihull
West Midlands
B91 3LT

6 February 2008

Dear Julian,

Re: **UNC Modification Proposal 186 and 186A – “Provision of Cost Information”**

Thank you for the opportunity to respond to these Modification Proposals.

Northern Gas Networks (NGN) agrees that it is beneficial to shippers to receive the information contained within these Modification Proposals. Forecasting likely price changes is a complex process, which is particularly difficult for smaller shippers with limited resources. Both Modification Proposals state that any Distribution Network (DN) information is prepared on a best endeavours basis, as an aid to shippers in their own forecasting processes, and that DNs are not be held accountable for any errors or omissions. NGN support this statement.

NGN does not support the implementation of Modification Proposal 186.
NGN gives qualified support however to the implementation of Modification Proposal 186A, subject to provision of legal text and provision of appropriate governance.

Rationale for not supporting Modification Proposal 186

The key difference between the two Modification Proposals relates to the forecasting of revenues after the end of the current price control period.

Modification Proposal 186 forecasts price changes for a rolling five year period and states:

“It is recognized that the relevant price control ends after 5 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.”

Modification Proposal 186A forecasts price changes to the end of the current price control period only and states:

“Each price control period normally lasts for 5 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.”

Modification 186 requires assumptions to be made about Allowed Revenue after the price control. The DNs would then publish their forecast of arithmetical price changes required to achieve that given assumed level of Allowed Revenue.

In the next two or three years in particular it would be difficult if not impossible to use anything other than arbitrary assumptions. NGN does 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. Whilst NGN would publish assumptions and caveats alongside the report, there is a significant risk that the values could be used out of context by individual shippers. Not only is there a risk that undue reliance could be placed on the entirely arbitrary Allowed Revenue calculations, there is also a risk that the assumptions used could be perceived to reflect NGN's view of an appropriate price control outcome. NGN would not wish to publish anything that could prejudice Ofgem's price control decision making process in any way.

Qualifications to NGN's support of Modification Proposal 186A

Not all shippers attend the DCMF meetings, and so it could be discriminatory to discuss possible outcomes of the next price control period with shippers at the Distribution Charging Methodology Forum (DCMF). Such discussion would be centred around any communication from Ofgem, and so in the early years it is expected that there would be relatively little that could be said about the outcome of the next price control.

All further qualifications below relate to Mod 186 as well as 186A.

There is a risk that, in particular smaller shippers, and new entrants to the industry, may not fully appreciate the levels of uncertainty around the values reported. DN forecasts of price changes vary as new information comes to light, and this report should be considered as providing little more than an indicative flavour of possible price changes. There is a risk that a shipper may become overly reliant on the forecasts published within this report and could make inappropriate business decisions as a result.

NGN considers that it would be more appropriate to combine the forecast of movements in cost pass through, incentives and K into a single aggregate value. This would provide a better forecast as directional uncertainties around individual items could be offset.

NGN agrees with the Proposer that this Modification can be implemented with immediate effect and that there will be no significant Transporter costs associated with this.

Yours sincerely,



Anna Taylor
Pricing Manager