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12th September 2011

Your Reference:UNC Modification Proposal 0382

Re: UNC Modification Proposal 0382:
Reducing the capacity element of LDZ system charges for SSPs.

Dear Bob,

Thank you for your invitation seeking representations with respect to the above Modification Proposal which National Grid Gas Distribution (NGD) would like to oppose.

Do you support or oppose implementation?

Support/~~Qualified Support/Neutral/Not in Support/Comments*~~ *delete as appropriate*

Please summarise (in one paragraph) the key reason(s) for your support/opposition.

NGD does not believe that implementation of this UNC Modification Proposal would improve cost reflectivity with respect to transportation charge recovery.

Are there any new or additional issues that you believe should be recorded in the Modification Report

NGD would challenge the extent to which sufficient analysis has been provided in support of this Modification Proposal.

Relevant Objectives:

How would implementation of this modification impact the relevant objectives?

We consider that this Modification Proposal, if implemented, would have a negative impact in respect of two of the Relevant Objectives which relate specifically to the Transportation Charging Methodology:

aa) That the charging methodology results in charges which reflect the costs incurred by the licensee in its transportation business

With respect to the relevant consultation on the move to a 95/5 capacity/commodity split in 2007, DNOs demonstrated that only around 5% of their costs (shrinkage and odorant costs) were related to throughput. It is now considered that only a small proportion of shrinkage costs are similarly related so that the overall proportion of costs related to such is significantly below 5%. Although some of the indirect costs do not directly relate to capacity provision, such costs are incurred in relation to the vast majority of direct costs which are capacity-related. We consider that changing the capacity:commodity split to 50:50 for Smaller Supply Points (SSPs) would produce a methodology which results in charges for SSPs which do not accurately reflect the costs incurred by the DNOs and which would reflect the costs less well than at present.

c) That the charging methodology facilitates effective competition between gas shippers and between gas suppliers

We consider that a move to a 50:50 capacity:commodity split for SSPs would result in the collectable level of revenue being strongly related to throughput whereas the price control Maximum Allowable Revenue for DNOs does not directly relate to throughput at all. Throughput levels for SSPs are strongly related to temperature. Introducing this change would be likely to lead to collected revenue levels in years when temperatures were not average (i.e. many years) which diverge considerably from the forecast collectable revenue when charges were set. This would lead to higher levels of under- or over-recovery (K) than with the current methodology which would lead to greater charge volatility and make charge levels less predictable than at present. Shippers have indicated recently that charge volatility and predictability is a significant issue for them. This change would have a detrimental impact upon such which could be considered to adversely impact on the facilitation of effective competition between gas shippers and between gas suppliers.

Whilst the levels of charges since the introduction of the 95:5 capacity:commodity split in October 2008 may be considered to be more volatile and difficult to predict than would be ideal, it is worth noting that the largest changes to charge levels in recent years occurred at October 2007, when the capacity:commodity split was 50:50 for all supply points, following a very warm winter in 2006/7. This generated significant under-recovery at April 2007 due to the strong throughput relationship. Although some colder than normal winters have been experienced since the introduction of the 95:5 capacity:commodity split at October 2008 the variation in throughput experienced has not contributed significantly to K levels, due to the 95:5 capacity:commodity split.

Impacts and Costs:

The costs of implementing this Modification Proposal would be expected to be insignificant.

Implementation:

What lead-time would you wish to see prior to this modification being implemented, and why?

On 1st April 2013 if an Ofgem decision is received on or before 1st February 2012; on 1st April 2014 if an Ofgem decision is received on or before 1st February 2013; or within 18 months following receipt if an Ofgem decision is received after 1st February 2013.

Legal Text:

NGD is satisfied that the text as published by the Joint Office within the Draft Modification Report meets the requirements of the Modification Proposal.

Is there anything further you wish to be taken into account?

No.

We trust that this information will assist in the compilation of the Final Modification Report.

Please contact me on 01926 653994 (alison.chamberlain@uk.ngrid.com) should you require any further information

Yours sincerely,

Alison Chamberlain
Network Code, Distribution