Issued 2nd November 2009.

Indicative Notice of LDZ Transportation Charges for North of England Distribution Network

To Apply from 1 April 2010

1 Introduction

This notice provides indicative levels of the LDZ transportation charges that will apply for the use of the Northern Gas Networks Limited (NGN) network from 1 April 2010, in accordance with the GT Licence requirements in Standard Special Condition A4, to provide 150 days' notice of such proposals.

The definitive notice of new distribution transportation charges from 1 April is expected to be published by 31 January, in line with the 60 days' notice requirements within the Uniform Network Code.

2 Indicative LDZ Transportation Charges effective from 1 April 2009

The indicative change in distribution transportation charges from 1 April 2010 is an increase of approximately 6.4%.

There is still uncertainty around the level of change that will be necessary in April 2010 and the figures provided are the current projections. This could move up or down before final changes in charges are published in January 2010.

Ofgem sets allowed revenue from April to March each year. NGN then has to set charges aiming to minimise any potential over or under recovery of revenue within the year. Usually prices can only be changed once a year. However, in order to avoid material over recovery, it was necessary to reduce prices on 1 October 2009. Therefore this price change occurs after a period of 6 months. The next price change after 1 April 2010 is expected to be in April 2011.

Consultation Paper DNPC05 (www.gasgovernance.com/industryinfo/TransportationCharges/Consultations/) proposes a rebalancing of the revenue recovery between LDZ System charges and Customer charges on a network specific basis, from April 2010. If this were to be introduced then the overall price change would be the same but the individual unit rates would incur different price changes. The equivalent unit rates that would be charged are shown in the appendix to this notice.

Distribution charges are approximately 15-20% of domestic supply prices. Therefore, a 6.4% increase in distribution transportation charges is equivalent to about a 1% increase on domestic supply cost. The extent to which any transportation charge is passed through to the consumer depends upon the shipper and the gas supplier.

The reasons for the level of change and the uncertainties surrounding the potential changes are explained in the following sections.

3 Reasons for Change in the Indicative Charge

Ofgem allows NGN to earn a specified Allowed Revenue in each year. A new five year price control settlement was agreed with effect from April 2008. This includes a decrease in the core Allowed Revenue of 4% including inflation, for the year April 2010 – March 2011 relative to the previous year, and so, all other things being equal, April 2010 unit prices would be expected to reduce in order to generate this lower level of allowed revenue. However, after adjustments, the reduction in Final Allowed Revenue is less than 1%. Prices were reduced by 5% in October 2009, and this, combined with the reductions in SOQs from 1 October 2009, has already reduced unit rates to below the level required to achieve the 2010/11 Final Allowed Revenue, and so an increase of around 6.4% is currently forecast. The final level of unit prices must also be adjusted to allow for a number of variables as described below.

3.1 Prior year adjustments

In October 2009, prices were reduced by 5% in order to generate appropriate revenues to achieve as far as possible our target of no material over or under recovery on Allowed Revenue for 2009/10.

The key drivers of this additional price change were the significant reductions in Shrinkage gas prices, coupled with reductions in the cost of our repex programme, which reduced NGN's allowed revenue such that an over recovery was anticipated for the formula year 2009/10.

This price change had to be set prior to the outcome of the October 2009 AQ Review process. The level of SOQs reduced by more than forecast, resulting in lower than forecast revenue, and so an under recovery is anticipated in April 2010 to bring forward into 2010/11.

3.2 Change in Business Rates

This cost is outside the control of Northern Gas Networks, and so is allowed by Ofgem as a cost pass-through item within the price control allowed revenue.

3.3 NTS Pensions payments

NTS has pension liabilities which were retained at sale and are now passed down to all the DNs and are allowed by Ofgem as a cost pass-through item within the price control allowed revenue.

3.4 Shrinkage

The price of gas is outside the control of Northern Gas Networks, and so has been separated from the core Allowed Revenue and allowed by Ofgem as an incentive mechanism within the price control allowed revenue.

3.5 Mains and Services Replacement Incentive

The distribution price controls are based upon an assumed cost each year for replacing distribution mains and service pipes. If a different mix of mains replacement activity is carried out, or if the activity is carried out more or less efficiently than assumed in the price control, this gives rise to a variation in the allowed revenue. The net position is difficult to forecast accurately as it depends on the length of pipe decommissioned for eight specific mains pipeline diameter bands and the associated services.

3.6 New adjustment items for the current price control

Four new incentives were introduced in the current price control. They are the Environmental Emissions Incentive, the Discretionary Reward Scheme, the Innovation Funding Incentive and the Loss of Meterwork Revenue Driver.

- The Environmental Emissions Incentive promotes reductions in methane emissions.
- The Discretionary Reward Scheme has a two year time lag and so will not come into force until 2010/11. It enables Ofgem to recognise projects relating to reducing environmental impacts, benefiting fuel poor customers or improving gas safety awareness.
- The Innovation Funding Incentive for sustainable development promotes investment in Research and Development.
- The Loss of Meterwork Revenue Driver reflects the impact of stranded costs within emergency service provision from any loss of meterwork contracts.

4 Uncertainties around Indicative Transportation Charges

The indicative price change may change (up or down) when final transportation charges are published at the end of January 2010. The main causes of potential variation between the final price changes and the indicative figures shown are changes in nominated capacities, gas prices, actual mains replacement and other incentives.

- Prices depend on the outcome of the October 2009 AQ Review process. In January 2010 the October 2009 levels will be known but the outcome for the 6 months from October 2010 will have to be estimated.
- The definitive mains replacement incentive position for 2009/10 will not be known until July 2010. This, together with any changes to the forecast mains replacement incentive position for the subsequent price control year, will affect the allowed price control revenue for 2009/10 and hence the under or over recovery and the price change required in 2010/11.
- Changes in wholesale gas prices will impact the Shrinkage Allowance.
- The revenue recovery levels also depend upon several other forecasts such as the number and mix of consumers. These forecasts will be updated before 31 January 2010 and will be taken into account in determining the definitive level of charges to apply from 1 April 2010.

APPENDIX

Consultation Paper DNPC05 http://www.gasgovernance.com/industryinfo/TransportationCharges/Consultations/ proposes a rebalancing of the revenue recovery between LDZ System charges and Customer charges on a network specific basis, from April 2010. If this were to be introduced then the overall price change would still be 6.4% but individual consumers may experience charges that are slightly higher or lower. The equivalent unit rates that would be charged are shown below.

Estimated Unit charges if network specific LDZ System charge and Customer charge revenue recovery splits are introduced.

Overall Unit charges are expected to increase by 6.4% from their current levels.

A consultation paper was published in early October 2009, regarding rebalancing the relative levels of Customer and System charges to be more cost reflective. As this rebalancing is primarily from one capacity charge to another, the overall price change would still be 6.4% but this would vary for individual customers depending on the relative value of their Customer and System charges.

If Customer charges were rebalanced to 28.8% of total charges, and overall charges were to increase by 6.4% this would generate the unit rates shown below. Please note that if this rebalancing does not take place then the indicative view of the System and LDZ unit rates would be the current published rates effective 1 October 2009, increased by 6.4%.

Directly Connected supply points

	Capacity	Commodity
	pence per peak day kWh per day	pence per kWh
Up to 73,200 kWh per annum	0.1354	0.0213
73,200 to 732,000 kWh per annum	0.1254	0.0197
732,000 kWh per annum and above	0.5951 x SOQ ^ -0.1806	0.1219 x SOQ ^ -0.2121
Interruptible customers 732,000 kWh per annum and above	0.2819 x SOQ ^ -0.1806	

Connected Systems

	Capacity	Commodity
	pence per peak day kWh per day	pence per kWh
Up to 73,200 kWh per annum	0.1354	0.0213
73,200 to 732,000 kWh per annum	0.1254	0.0197
732,000 kWh per annum and above	0.6292 x SOQ ^ -0.1939	0.1163 x SOQ ^ -0.2131
Interruptible customers 732,000 kWh per annum and above	0.2981 x SOQ ^ -0.1939	

LDZ Customer Capacity charges

	Capacity
	pence per peak day kWh per day
Up to 73,200 kWh per annum	0.0743
73,200 to 732,000 kWh per annum	0.0026
732,000 kWh per annum and above	0.0567 x SOQ ^ -0.2100

LDZ Customer Fixed charges - 73,200 to 732,000 kWh per annum only

	Fixed
	pence per day
Non-monthly read supply points	23.3913
Monthly read supply points	24.9065