

Gas Distribution Price Control Review Seminar

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23 January 2007

Agenda

- Purpose:
 - To consider issues relating to GDPCR and assess how proposals affect customers
- Session 1 -10.00 to 11.30
 - Key issues raised in the third consultation document
 - Northern Gas Networks view
 - Centrica view
- Session 2 – 11.45 – 12.30
 - Ensuring that GDNs meet consumers needs
 - Q&A panel session
 - Closing remarks
- Sandwich lunch next door

Gas Distribution Price Control Review

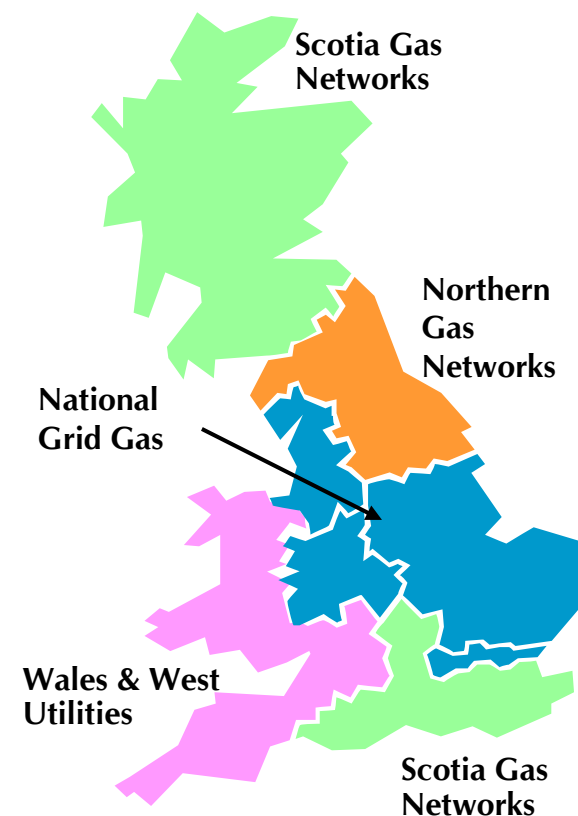
- External Context
 - DN sales
 - PAC report
 - Mod 90 and 116
- GDPCR Process
 - Some issues dealt with in 1 year review
 - Authority committee
- Overall approach to price control reviews
 - Consistency
 - Cost reporting
 - Focus on investment
 - Output measures
 - Quality of service

Key issues raised in the third consultation document

Joanna Whittington – Director, Gas Distribution

Gas distribution networks

- Regulatory asset value of GDNs approx £11.4 billion
 - as at April 2007, 2005-06 prices
- Total allowed revenues of approx £2.3 billion per annum
 - 2007-08, 2005-06 prices
- 15% per cent of an average domestic consumers bill



GDPCR deliverables

- To reset GDNs' revenue allowances from 1 April 2008, and to...

Introduce a framework for maximising the customer benefits available from comparative competition

- cost reporting
- measurement of quality of service outputs

Focus on GDNs better meeting the needs of customers from both a management & regulatory perspective

- passing back efficiency savings
- new incentives on companies

Develop long term solutions for issues which have emerged during this price control period

- incentives on interruption and offtake
- accuracy of pipeline records

Outputs and Incentives

- As well as assessing costs, it is also necessary for the price control to specify outputs
 - What services will the network provide using its allowed revenue?
 - Are these services what customers want?
- Incentive mechanisms affect the amount of revenue a network may recover
 - designed to influence networks' behaviour in a way that protects the interests of consumers

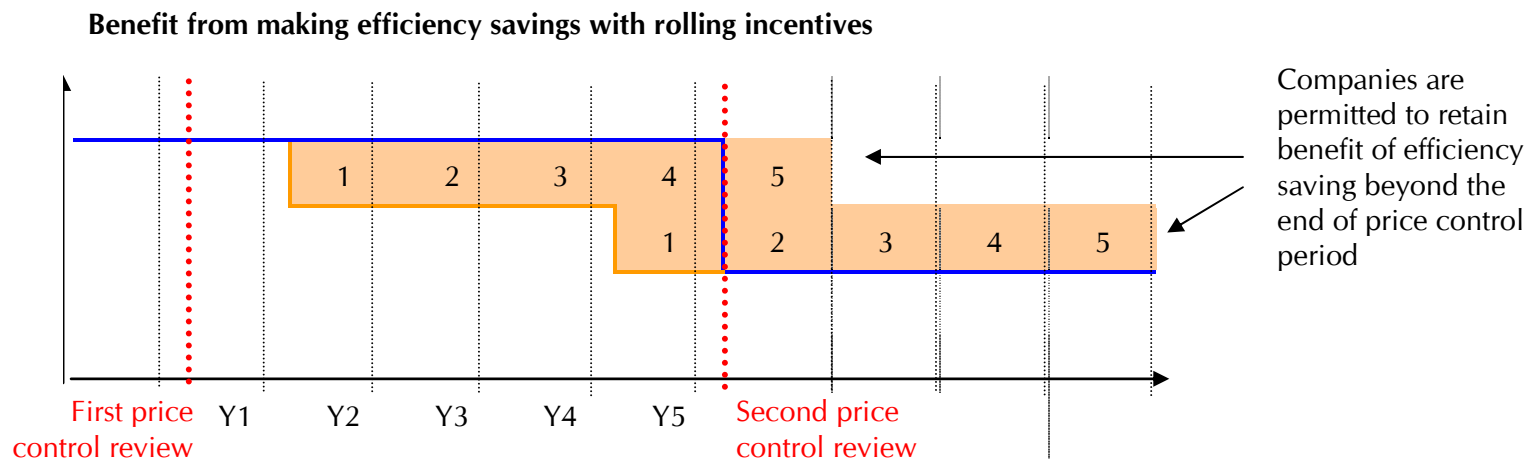
Outputs and Incentives

- Some of the incentives and output measures being considered as part of GDPCR:
 - rolling incentives
 - information quality incentive
 - mains replacement incentive
 - capacity output incentive
 - accuracy of pipeline records incentive
 - corporate social responsibility
 - network extensions

Quality of service incentives will be discussed in Session 2

Rolling incentives

- Under a basic RPI-X regime, incentives for efficiency are stronger at the beginning of the price control period
- Rolling incentives are designed to ensure that companies are neutral about the timing of expenditure over the course of the price control



Information quality incentive

- Companies have an incentive to game the regulator in price control submissions
 - companies consistently argue that the easy gains have been achieved
- Information quality incentive encourages companies to provide reasonable capex forecasts
 - increasing reward for companies that choose a low cost allowance

Do you agree with our initial view that a capex rolling incentive and information quality incentive should be implemented?

Mains replacement incentive

- GDNs' allowed revenue varies in accordance with type and quantity of mains replaced
- Problems have arisen due to:
 - forecasting uncertainties of the diameter mix of pipes leading to fluctuations in revenue
 - relative strength of the incentive vs general capex
- Support retaining incentive but with amendments

Should we retain the mains replacement incentive?

Capacity outputs incentive

- Networks need to balance investment between:
 - their own network investment, investment in storage, paying to interrupt customers and purchasing NTS offtake capacity.
- Previously this relationship was internalised within Transco
- Need to encourage trade off and avoid risk of remunerating twice or providing perverse incentives to defer necessary investment
- Capacity output incentive to address these concerns and incentivise networks to trade off between the outputs to minimise overall costs

Accuracy of pipeline records incentive

- Concern over the accuracy of pipeline records
- This impacts on:
 - efficiency of GDNs and ability to operate safely
 - competition in connections
- Complex area but looking to incentivise improved quality of records

Should we incentivise accuracy of pipeline records?

Corporate social responsibility

- Consideration of discretionary reward scheme
- In electricity distribution focus is priority customer care, corporate social responsibility and wider communication strategies.
- In gas distribution examples could include:
 - network extensions
 - Education about the dangers of gas, provision of approved carbon monoxide detectors to customers etc

Should we establish an incentive scheme that recognises GDNs' corporate social responsibility initiatives?

Network extensions

- In addition to discretionary reward scheme, we are considering options to facilitate network extensions
- Network extensions facilitate lower emissions of carbon dioxide and also lower heating costs
- Connecting customers face network connection costs and also in-house works
- Consideration being given to charging structure and incentives

Should we establish special charging arrangements and/or an incentive scheme to promote network extensions?

A large, central version of the ofgem logo is positioned in the middle of the slide. It features the word "ofgem" in white lowercase letters on a red rounded rectangular background. The background of the slide is a faded, blue-tinted image of electrical components, including a three-pin plug and a fuse box, which are partially visible on the left side.

Promoting choice and value for all
gas and electricity customers