

Cheryl Mundie, Senior Manager - Transmission  
Ofgem  
Cornerstone  
107 West Regent Street  
Glasgow  
G2 2BA



1 December 2009

Dear Cheryl,

### **TAR – Enhanced transmission investment incentives – Initial proposals**

EDF Energy welcomes the opportunity to respond to this consultation on Enhanced Transmission Investment Incentives. The key messages of our response are as follows:

- **EDF Energy believes that efficient transmission investment is a primary factor in ensuring the timely connection of renewable and low carbon generation, which in turn will contribute to the delivery of Government policy objectives on energy and carbon emissions.**
- **It is therefore essential that the investments identified and agreed by the Electricity Networks Strategy Group (ENSG) are progressed as a priority. It is our understanding that the network solutions proposed by the ENSG (using National Grid's Gone Green scenario) are robust under various scenarios proposed since this work was completed.**
- **We support the proposal to release pre-construction costs identified within this consultation and welcome the proposed release of £190m within the current price control for construction funding.**
- **We urge Ofgem to assess the remaining projects in a balanced way (taking account of constraint costs if the network is not built in time) and then to provide the necessary funds accordingly.**

### **Introduction**

The next few years of generation and transmission investment will be critical in setting the foundations for the period 2020 – 2050. Efficient transmission investment is a primary factor in ensuring the timely connection of renewable and low carbon generation, which in turn will contribute to the delivery of Government policy objectives on energy and carbon emissions. It is imperative that the progress Ofgem has made to date in releasing funding for strategic transmission investment is maintained now and in the next price control review.

To agree the level of strategic investment required for 2020 the ENSG considered National Grid's 'Gone Green' scenario. There are now extensive potential scenarios which have been developed to understand the implications of meeting Government's 2020 targets and beyond, but there is no evidence to suggest that the strategic investments identified will not be required under any of these other scenarios.

## Initial proposals

EDF Energy agrees that those projects where valuable pre-construction work can be undertaken under the current price control should receive the funding for this work.

We fully support the intended release of £190m for construction costs within the current price control and welcome Ofgem's intention to conduct an assessment of need in determining whether to release funding to Transmission Owners (TOs) for individual investment projects. In materiality terms, this represents only one fifth of the projects for which funding on early timescales has been requested by TOs. We urge Ofgem to appraise the remaining projects with the full understanding of potential constraint costs if the network is not built in time.

## Assessment of investment projects

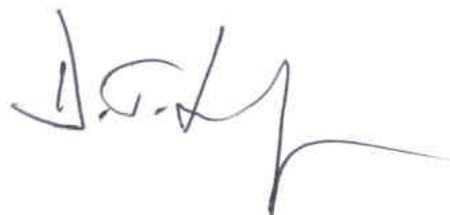
Subject to the findings of the review by Ofgem's consultants of each TO proposal, all projects which can enter construction within the current price control and which are likely to be utilised over the network asset's lifetime should receive full funding. Given that the proposals being consulted on provisionally allow only £200m out of £978m of the TOs' proposals during the current TPCR, there appears to be some risk that Ofgem's consultants may be taking an unduly restrictive approach to project appraisal. The potential constraint costs that may arise if the transmission assets are not constructed mean that it is important that an appropriate and timely approach is taken to funding transmission works.

Historically, the cost of transmission has been said to be 10% of the cost of generation – investment in new generation in the UK by 2020 will have total capital costs of £100billion<sup>1</sup>. The risk of increased operational or constraint costs appears more material than the risk of under-utilised transmission and the very long life of transmission assets might suggest that investments may be more highly utilised in future. These considerations should be part of the assessment of individual projects.

A very short-term approach to funding new transmission construction costs, for example year-by-year, would not work well, in view of the need of the transmission firms for stability; however, subject to this, it may be necessary for Ofgem to retain some flexibility.

Our detailed responses to your questions are attached. If you have any queries on this response or would like to discuss further, please do not hesitate to contact Rob Rome on 01452 653170, or myself.

Yours sincerely

A handwritten signature in black ink, appearing to read 'D. Linford', with a long horizontal flourish extending to the right.

**Denis Linford**  
Corporate Policy and Regulation Director

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<sup>1</sup> As estimated by the government's Renewables Advisory Board

## Attachment

### TAR – Enhanced transmission investment incentives – Initial proposals

EDF Energy's detailed response to specific questions.

#### CHAPTER: Two

**Question 1: Do respondents consider we have appropriately summarised the views of respondents to our September consultation?**

Yes, your general representation of our views is reasonable.

**Question 2: Do respondents have any comments on the initial findings of our consultants or views on the issues raised by the TOs?**

We would not feel knowledgeable enough to comment on specific project proposals. All projects which are likely to be able to commence construction within the current price control and are likely to be utilised should receive full funding. The potential constraint costs that may arise if the transmission is not constructed on time means that funding costs should be considered holistically, i.e. in terms of total costs rather than capital costs only. The cost of transmission has historically been said to be typically 10% of the cost of generation and the risk of increased operational costs appears more material than the price risk arising from under-utilised transmission.

#### CHAPTER: Three

**Question 1: Do respondents have any comments on our proposed funding framework for additional investment within TPCR4?**

We are broadly supportive of the proposals and would be happy to see TPCR4 expediently extended for one year.

**Question 2: Do respondents have any views on the appropriate funding mechanism for provision of pre-construction funding ?**

No, we think it is wise to fund all the preconstruction work mentioned in the consultation to the end of 2011/2012. Preconstruction work is of very low materiality compared to actual construction work but is of significant value to transmission owners.

If the price control period is extended to 2012/2013 then funding for all preconstruction work identified in relation to 2012 / 2013 should be released as part of the final year's arrangements.

**Question 3: Do respondents have any views on our proposed approach to identifying projects eligible for construction funding?**

As we have previously stated, the risk of increased operational costs appears more material than the risk of under-utilised transmission and the very long life of transmission assets might suggest that investments may be more highly utilised in future. These considerations should be part of the assessment of individual projects.

**Question 4: Do respondents have any views on our proposal to fund construction costs up to the end of TPCR4 for specific projects? Do respondents agree that it may be appropriate to provide funding up to an earlier end date for projects in certain circumstances?**

See our replies to chapter two question two, and chapter three, question two.

**Question 5: Do respondents agree that the same rate of return should apply as for other investments undertaken within TPCR4?**

Yes – this is allowed expenditure and incurs no special risk, for example no risk of disallowance if initially under-utilised compared to forecast.

**Question 6: Do respondents have any views on the appropriate treatment of projects beyond TPCR4 or on any interaction with our decision on the timing of TPCR5 ?**

We agree with Ofgem that an incentive-based approach to TPCR4 investment might have the opposite effect to that intended and lead to delays and/or higher costs of finance. However, while we understand Ofgem’s wish to allow for the possibility of a different treatment of projects beyond TPCR4, we would be concerned that any lack of continuity over the TPCR4/5 transition could lead to a delay in agreeing TPCR5 funding. We would therefore urge Ofgem to consider carefully the consequences of delaying ENSG agreed ‘least regrets’ TPCR5 investment decisions until the commencement of the TPCR5 formal price control review process and, where appropriate, extend their TPCR4 approach to projects that will begin early in TPCR5.

**Question 7: Do respondents have any comments on any other aspect of our Initial Proposals?**

No.

**CHAPTER: Four**

**Question 1: Do respondents have any views on our proposed approach for taking forward our work on TO incentives to facilitate further investment within the current transmission price control?**

We have no further comments beyond those made in response to the Chapter Three questions.

**Question 2: Do respondents have any views on our proposed consultation process going forward?**

No

**EDF Energy  
December 2009**