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RIIO-T1: Initial Proposals for National Grid Electricity Transmission and National Grid Gas July 2012

Dear Grant

Thank you for the opportunity to comment on these Initial proposals. This response is provided on behalf of the RWE group of companies, including RWE Npower plc and RWE Supply and Trading GmbH.

The Initial Proposals define outputs that National Grid Gas Transmission (NGG) and National Grid Electricity Transmission (NGET) must deliver over the eight-year RIIO-T1 period 2013-2021. NGET and NGG have requested significant funding to deliver these outputs, but both TOs face considerable uncertainty over the size, location and timing of when they will need to undertake any investment. To reflect the uncertainty, the price control framework contains a mix of ex ante, baseline allowances, together with a range of uncertainty mechanisms that will trigger additional funding over the period.

Given the scale of the investment proposed, asymmetry of information and lack of effective comparators, especially in gas transmission, we generally endorse the challenges to Totex and the broader financial parameters proposed by Ofgem.

We still believe that the scale of NGET's proposed expenditure warrants further debate around alternative baseline scenarios that could credibly deliver the 2020 targets while minimising asset stranding risks for consumers. Until Project TransmiT has been concluded, efficiencies in the future development requirements of the power system may not be optimised. For NGG, we note that the approach is for expenditure on incremental capacity to be remunerated in response to user signals rather than funded as an ex ante allowance. Absent these user signals, consumers would only fund baseline Totex, as the uncertainty mechanisms would not be triggered.

However, there is a trade-off between uncertainty mechanism and ex ante Uncertainty mechanisms, together with the range of incentives and other adjustment mechanisms mean that the actual level and profile of annual allowed revenue of will not be stable. There is clearly a linkage between revenue stability and charging predictability and we believe that the main impact on shippers and suppliers of the proposals will be uncertainty and volatility in transportation charges. National Grid may need to provide more frequent updates of its revenue

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recovery against allowed revenue, together with any changes to revenues that may lead to a mid-year tariff change. We also await the conclusion of Ofgem's work on mitigating network charging volatility. Agreeing a suitable mechanism for predictable and transparent transmission charges for setting tariffs is a key supplier requirement.

The implementation of RIIO-T1 creates a problem for suppliers. As suppliers, we are very concerned that the release of Final Proposals is later than the date when Network Operators release Indicative Tariffs. The impact of this is that Network Operators will be forced to publish Indicative Tariffs using revenues which are likely to be different to those used in the Final Tariffs. This will result in potentially large differences between Indicative and Final tariffs.

We would request that Ofgem bring forward the publication of revenue information in time for Network Operators to use it in both Indicative and Final Tariffs. If this is not possible, we would request that Ofgem agree revenue with the Network Companies that is used in both Indicative and Final Publication. Any changes to these revenues should then be adjusted from future years' revenues when Final Allowed Revenues are known. We would also urge Ofgem to ensure that this situation is not repeated in RIIO-ED1.

We support Ofgem's approach to setting NGG's incremental capacity output for 2013/14, pending development of an enduring Capacity and Connections solution. NGG and the wider industry continue to discuss the commercial and regulatory changes required to align the connection processes with timescales implied by the Planning Act 2008. As an industry, we need to work hard to ensure that this process facilitates timely infrastructure investment in the GB market.

NGG and NGET have argued for additional resourcing to support market facilitation activities, notably increasing EU interaction. We need to understand better the EU role and how it interacts with current GB market facilitation activities. In particular, GB market participants are already funding their own EU lobbying and representation and it needs to be clear whether National Grid will be pushing forward its own or its customers' interests.

We agree with Ofgem's view that a specific uncertainty mechanism should not be afforded to National Grid in relation to steel/copper prices and that managing this risk should be a core competence for National Grid.

IMPACT ASSESSMENT

The Impact Assessment sets out the expected qualitative benefits and risks from implementing the RIIO price control on NGG and NGET. Against a background of increased network investment, Ofgem conclude that RIIO will lead to network charges that, on average, are less than those that would have arisen under the previous RPI-X framework. Clearly this outcome is not easily demonstrated and the post-implementation review will have a key role in evaluating the net benefit from implementing RIIO.

We hope these views are helpful and if you wish to discuss any aspect of them in further detail, please do not hesitate to contact me.

Yours sincerely,

By email so unsigned

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