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17 November 2003

Dear

TIMETABLES FOR PRICE CONTROL REVIEWS

1. As you will know Ofgem issued consultation papers in June 2003 and July 2003 that discussed the timetable for setting price controls. The majority of those respondents that commented on these issues recognised that there would be advantages in aligning electricity and gas transmission price controls, provided that the Ofgem could ensure a smooth transition to the new arrangements. This would involve two year extensions to the Scottish transmission price controls and a one year extension to NGC's electricity transmission price control, so that new price controls would commence simultaneously for all these activities in April 2007. This would allow GB wide transmission issues to be considered together (including cost allocation issues for NGT) and Ofgem intends to proceed on this basis.
2. In February 1998 and March 1998 OFFER issued short consultation and proposals papers on a one year extension to the Scottish transmission price controls. The decisions on these controls were based on a broad assessment of costs and returns, aimed at balancing the interests of consumers and providers of finance.
3. Similar considerations are likely to apply in relation to extensions to the existing electricity transmission price controls. While a full price control review would not be appropriate or proportionate it would be important to ensure that the interests of consumers are adequately protected and companies can finance their licensed activities. This suggests assessing performance against the assumptions underlying the present price controls and in broad terms the likely level of costs and returns over the period of the interim controls.
4. There will be a number of interactions with other work programmes to consider. First, the important matters relating to additional capital expenditure to facilitate the connection of renewable generation. Work has already started on these matters with the

publication of a consultation paper in October 2003. This should help inform the wider review of capital expenditure that will be a necessary part of the work needed to extend existing price controls and so these two work programmes should complement each other.

5. The work on the Scottish transmission price controls will need to encompass work on setting separate system operator (SO) and transmission operator (TO) components for BETTA. All three price controls will need to take account of the implementation costs associated with BETTA as well as the prospect of future cost savings arising from BETTA.
6. In addition to the matters set out above it will be appropriate to consider whether to extend the gas distribution price control by one year. This would have considerable advantages in terms of providing a more balanced work load by delaying the implementation of the next gas distribution price controls until April 2008 and allowing gas transmission and distribution issues to be considered separately, as is the case in electricity. However, as this change in the timetable was not dealt with in detail in the June 2003 and July 2003 consultation papers it is appropriate to seek views on a wider basis before confirming these new arrangements.
7. I should be grateful for any comments on the issues set out in this letter by 19 December 2003.

Yours sincerely

DAVID GRAY
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