



taking care of the essentials

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Our Ref. Price Controls & Incentives

Your Ref.

1 December 2003

Dear Mr Haldearn,

Price Controls and Incentives under BETTA - an Ofgem/DTI Consultation

Centrica welcomes the opportunity to provide comments to Ofgem/DTI on their consultation concerning the setting of price controls and incentives under BETTA.

As a general point, we suggest that Ofgem needs to ensure that any price controls and incentive schemes applying to NGT are as transparent and open as possible. It is essential that controls do not contain any perverse incentives on the company to act in a specific manner to optimise their position to the detriment of either the industry or the other two TOs.

Furthermore, we suggest that as an optimal solution, NGT should be separated into two entities: GB SO and TO. Any interactions between these two entities needs to be open, transparent and auditable. However, we note with disappointment Ofgem/DTI's ongoing intention for the STC to contain a section for the combined SO/TO, if this is implemented, it would obviously be impossible for NGT to be divided into two separate entities, however, the relationship between the two sections must still be as open and transparent as possible.

We agree with Ofgem that NGT's existing price control and incentive scheme should form the basis of the price control and incentive scheme under BETTA. We also agree that only minor changes should be required to these schemes in the short term. Although, we can appreciate that when transmission access arrangements are implemented, work on moving to a deeper SO incentive scheme will be required.

Care needs to be taken by Ofgem in setting the levels of any increment to NGC's revenue restrictions. For any Part 1 increment, we suggest the total revenue restriction should, as a maximum, be the combined current restrictions for all three TOs taking into consideration the RPI-X levels. We understood from previous documents that it would be the responsibility of the GB SO to collect, and distribute accordingly, all the revenue associated with the three TOs. Any incremental revenue associated with the setting of the SO incentive scheme, should, we suggest, be very closely monitored and Ofgem should exert pressure in this area to ensure that the maximum cost savings flowing from economies of scale can be realised in the shortest timescales possible.

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We agree that Ofgem need to carefully consider the treatment of any revenue flowing into the "K" factor at the end of the separate price controls. It is vital that any over/under recoveries are eliminated via the appropriate users.

Centrica suggests that a greater degree of transparency and visibility of NGC's costs is required going forward. As part of the process of setting incentives, NGC provides forecasts of their future costs; this is then used to set the levels for the target costs. We firmly believe that this part of the process should be more tightly controlled, this is especially the case as:

- ◆ Going into a period of certainty over the costs associated with being the GB SO, the forecast level of these costs is likely to err on the upper end of the range, if only for commercial reasons.
- ◆ Historically, NGC have easily met their target costs, and over the last two years have been substantially rewarded via incentive payments for reducing costs based on targets set using these forecasts.

We suggest that Ofgem should exert a tighter control over the level of these costs with more information and justification of forecast costs being provided by NGC. We also suggest that the GB SO should be firmly encouraged to reduce the long term ongoing costs.

Although we consider that it is appropriate for income adjusting events (IAE) to be considered under the price controls and incentive scheme, we suggest that more information must be provided to the industry to allow for these to be raised in both positive and negative directions. Currently, we suggest that only NGC have the appropriate information to be able to raise an IAE, this results in IAEs only being raised for Ofgem's consideration in NGC favour.

We support Ofgem's suggestion that all the price controls and incentive schemes should be aligned. We further support the proposed timetables for the necessary consultations due before the April 2005 implementation of BETTA and the contingency timetable if the implementation is delayed.

Although we appreciate that some costs may not have been finalised at BETTA go-live (implementation costs etc) and that these may have to be reflected within the price controls at a later date, we believe that there should be a cut off date for any adjustments of this sort to be made.

I hope these comments have been of use and please contact me if you require any further clarification.

Yours sincerely,

Sarah Owen
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