



**CHEMICAL INDUSTRIES
ASSOCIATION**

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**TRANSMISSION PRICE CONTROL REVIEW
INITIAL CONSULTATION**

Dear Robert

The CIA welcomes the opportunity to respond to this important consultation. We welcome the fact that Ofgem is reviewing the price control of all four transmission businesses at the same time. We are further encouraged that Ofgem is conducting this price control review with customer protection, transparency and accessibility as their core objectives. In particular the CIA believes that:

- The best way to address the external factors of closer linkage between the gas and electricity markets is to review the price control of all four transmission businesses at the same time. This should identify areas of investment across the various networks that are being driven by this greater interaction, and so ensure a price control is adopted that ensures the most economic and efficient allocation of resources.
- It may be possible to incorporate the expected increase in distributed generation into the price controls, the impact of renewable generation is much harder to address. Whilst the long lead times for renewable generation should help National Grid identify which onshore reinforcements will be required, and so be incorporated into this price control; the DTI and Ofgem are still consulting on how best to regulate offshore transmission. The CIA therefore believes the best way to approach this issue is to incorporate the onshore reinforcement costs into National Grid's price control, and a second scenario should be prepared in the event the National Grid becomes responsible for the "Offshore Transmission Network". Preparing for this eventuality at this stage will allow for the development of a full proposal that is transparent, accessible and will incorporate the views of industry at this stage.
- The impact of GB moving from being a net exporter to net importer of gas should only impact the price controls when forecasting the required capital expenditure that will be required for these new import projects, and Transco's regulated returns from this investment. Further given that all of the expected import projects have been undertaken for commercial reasons the CIA would expect the developers to fully bear the reinforcement costs directly associated with these projects.
- The standard five-year model and RPI-X indexation remains appropriate for the next transmission price controls. Given the complexity of these price controls and the fact that four transmission businesses are being assessed all simultaneously we feel that a



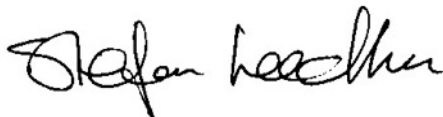
CIA members are committed to Responsible Care

five year period is optimal, with Ofgem having the ability to reassess these controls at any point during this period if there are any significant unexpected changes. Further the CIA does not envisage any requirement to adopt an alternative model.

- The interests of all classes of consumers and users of the transmission businesses are best served by ensuring that the operators of these businesses operate as efficiently and economically as possible. A key driver for all competitive businesses is to reduce costs, and the CIA therefore believes that the price control incentives should balance efficiency and maintain the current infrastructure to ensure our members have access to reliable networks. This is the only way to ensure that the monopolies strive to operate as economically and efficiently as possible, whilst reducing costs and providing the level of service required of its customers.
- Rolling incentives are appropriate for transmission and the retention period for efficiency savings should be five years. This will ensure that transmission operators have an incentive to reduce costs throughout the price control period and not just when they are initially implemented. Further the CIA believes that it would be appropriate for the retention period to be the same length as the price control period to ensure any savings made at the end of one price control period and evenly spread over the following period.
- By ensuring the strength of incentives for efficiency in operating costs and capital costs are equalised any perverse incentives, which could inhibit overall efficiency, would be removed. This will ensure that cost savings are explored and identified in both areas, and not concentrated on cost savings that have stronger incentives.

If you have any questions about any of the comments made in this representation please contact me.

Regards

A handwritten signature in black ink that reads "Stefan Leedham". The signature is written in a cursive, flowing style.

Stefan Leedham
Business Analyst, Chemical Industries Association