

Robert Hull
Director, Transmission
OFGEM
9 Millbank
London
SW1P 3GE

Ferry Road
Grangetown
Cardiff/Caerdydd
CF11 0XR
T:029 2076 7600
enquiries@wwutilities.co.uk
www.wwutilities.co.uk
24 hour gas escape number
Rhif 24 awr os bydd nwy yn gollwng

0800 111 999*

*calls will be recorded and may be monitored
caiff galwadau eu recordio a gellir eu monitro

9 September 2005

Dear Robert

Transmission Price Control Review OFGEM Initial Consultation

Wales and West Utilities (WWU) have the following comments on the above consultation paper.

Whilst WWU is the Gas Transporter for Wales and the South West of England and does not own or operate a transmission system, a number of regulatory price control policy matters are raised in the document. These are considered relevant in the context of the setting of monopoly price controls including those for Gas Distributors, whose price control review is due to commence in the near future.

Chapter 4 Framework, context and objectives

One area that the workstreams on the review of monopoly price control spent some time looking at is the issue of periodicity, particularly in respect of operating costs. The question of periodicity arises when considering the power of the opex incentive in relation to the timing of costs savings. At the start of the normal quinquennium operating cost savings can be retained for five years. However the incentive weakens throughout the price control period to leave little or no incentive towards the end as savings are only retained for a short period. Of course this is all dependant on the methodology used in setting price controls but without foreknowledge of the methodology OFGEM intend to employ in the forthcoming GDPCR1 it is assumed the issue of periodicity remains.

The issue has been recognized through a number of OFGEM documents such as the Final proposals on Monopoly Price Controls and the Electricity Distribution Price Control. All these documents have stated that as a matter of principle five year rolling retention periods would be introduced. In relation to gas price controls, the letter from Andrew Walker entitled Gas Distribution Price Controls set out OFGEM's present thinking on appropriate incentives for operating and capital expenditure efficiencies. In particular OFGEM stated that those principles are likely to include the retention of benefits of efficient underspend for a period of five years.

The Transmission Price Control consultation paper states that OFGEM will seek to use rolling 5-year retention periods for efficiency savings in both operating and capital expenditure (4.5). However the paper goes on to note in 4.45 that due to informational concerns and the scope for gaming OFGEM did not implement an operating cost rolling mechanism for the electricity DNOs.

Whilst recognising these concerns WWU believes these can be properly and fully addressed through clearer annual mechanisms such as the regulatory reporting returns recently introduced for the electricity DNOs. We have a licence condition requiring us to introduce similar returns, and would like to move forward on the development of such returns as soon as possible, providing that the agreed principles of using 5-year rolling retention mechanisms are continued. WWU is willing to work constructively with OFGEM to address the information and gaming concerns in the forthcoming GDPCR1 and sees the regulatory reporting framework as the means to overcome them. We also believe that there are important customer benefits to be achieved from rolling retention, especially the earlier introduction of efficiency improvements and the eventual impact on customer charges,

Chapter 6 Incentives

Thinking is still being developed on DN level incentives, and we would wish to see this aligned with whatever emerges from the discussion of transmission level incentives. In particular:

- the same baseline process should apply across Transmission and Distribution PCRs
- there needs to be consistency between incentives. For example, if Transmission incentives are based around outputs at nodal level (Offtake point) and System Operator incentives at zonal level (Offtake grouping), this may cause conflict between planning and operation of the network. We (informally) use a zonal approach to operation currently which allows the network to minimise shrinkage costs and maximise metering accuracy in the summer months.
- whilst we accept that the Interruption algorithm exists to manage site selection in a non-discriminatory manner, it is important to ensure that in all cases the incentives are neutral, for example that they do not encourage or discourage NTS level interruption at the expense of DN level interruption, nor that there is any discretion that would favour one DN at the expense of another.

If you wish to discuss this response please contact bob.westlake@wwutilities.co.uk on 02920 588290.

Yours sincerely

Bob Westlake
Regulation Manager