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### **Transmission Price Control Review – Updated Proposals September 2006**

Dear Robert,

We welcome the opportunity to comment on the issues raised in this Transmission Price Control Review Updated Proposals consultation. This response reflects the views of RWE npower and the UK based business of RWE Trading GmbH.

#### **General Comments**

The focus of attention of these updated proposals is the allowances that Ofgem intends to provide to fund the efficient expenditure of the network owners over the next price control period. As such, we believe it is for the transmission licensees to provide detailed responses to the questions raised in the consultation.

We recognise that the overall framework has been developed against a background of changing patterns of energy supply and demand leading to increasing investment uncertainty. The proposals have been designed to manage this uncertainty with the introduction of mechanisms for adjusting capital expenditure and revenue allowances in response to user commitments to underwrite, in part, any investment. In turn this has created an increasingly complex regime and arguably an increased role for Ofgem as the final arbiter of the efficiency of investment decisions. As network users, we require timely and efficient network investment and continue to believe that the new price control framework should align the incentives between the providers of monopoly transmission capacity and infrastructure developers requiring connection to it. Where there is continued misalignment, then the risks need to be allocated correctly between the parties. It is not easy to assess whether these new arrangements will meet our requirements in this regard.

Where these price control proposals do impact us as network users is how the arrangements for

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user commitment, network access and capacity booking are transposed into the key commercial industry codes and agreements. We have the following observations on the proposals set out in Chapters 9 and 10 of the consultation.

## **Chapter 9 - Adjustment Mechanisms and Incentives: Electricity**

In our response to the June Initial Proposals document, we indicated our broad support for the approach set out by Ofgem and this remains the case in the light of these Updated Proposals. We await Ofgem's further proposals for the Innovation Funding Scheme as it is still not clear to us the nature of the technical challenges that transmission owners will face in the next five years.

As noted in the general comments, the key impact for us is how the price control proposals interact with reforms to the access arrangements. Revised access arrangements that reflect the principles of user commitment still require significant detailed development, which is only just beginning. It is of concern that given where we are in the process, there is still scope for revisions to the incentives faced by NGET, SPTL and SHETL as a result of these ongoing industry discussions. In view of the fundamental nature of the regime changes and the potential commercial impact on both the licensees and network users, adequate time must be given to understand fully how the arrangements will work in practice.

## **Chapter 10 - Adjustment Mechanisms and Incentives: Gas**

### ***Entry Capacity***

Our preference would have been for a fundamental assessment of the gas entry capacity arrangements at the outset of the TPCR. This would have allowed an empirically based process of regime development rather than what appears to be a more piecemeal approach. Notable here is the sudden introduction of the "lead-time extension permits" that weaken the additional incentives, via a strengthened buy-back regime, on NGG NTS to deliver incremental capacity that were introduced in the Initial Proposals document. These permits need more development and it is difficult to comment at this stage on whether the 30GWh for 365 days is appropriate. One potential impact is that different projects may be treated differently depending upon whether NGG NTS has used all its permits or not. If it has, then any delay to delivery of infrastructure will be subject to buy-back; if not, then the use of the permit will avoid NGG NTS being required to buy back capacity. This could be considered discriminatory. We are also concerned about NGG NTS being able to earn credits through shorter lead times as some projects may not need any investment at all.

Absent this fundamental review, we welcome Ofgem's proposals for minimal change to the entry capacity regime and agree with the retention of baselines and the obligation to release baseline to apply up to within day as this creates stability and does not undermine existing capacity purchases made in earlier long-term auctions.

### ***Offtake Capacity***

There are a number of areas that require further development and definition. For instance, NGG NTS has yet to publish any information on how exit (flat and/or flex) baselines would be adjusted to reflect changes at entry, and vice versa. Also, Ofgem has still not commented on whether they think a 4 year user commitment and a 15 month notice to reduce prevailing rights is appropriate, particularly in light of the recently published Marchwood determination.

Paragraph 10.18 implies that the reasonable endeavours obligation to transfer capacity applies at both entry and exit. However, the document only makes reference to how this might work at entry and NGG's modification proposal 0116: Reform of NTS Offtake Arrangements does not provide for exit (flat) transfer between exit points. We have previously expressed doubt about whether a transfer obligation is necessary or appropriate at exit and have already commented on these proposals as applied to entry capacity.

Whilst we agree that it is appropriate to set default lead time at exit (and entry) this should not preclude bi-lateral arrangements between shippers and NGG NTS based on shorter timescales. It is also unduly restrictive to stipulate an October gas year start date and we believe that providing the level of user commitment is commensurate with that prevailing under enduring arrangements any start date could be agreed.

### ***Capacity Substitution***

While the proposed substitution obligations are correct in principle we remain to be convinced that they will be practical in reality. As described, the substitution mechanism will be very complex, with an Ofgem-approved methodology together with further Ofgem approval of any actual baseline substitutions. It is not clear the extent of any over or under-recovery that is likely to result under this mechanism and the consequential increase in SO transportation charge volatility. In our view, much work remains to be done to establish the methodology and transparency of process to provide confidence to industry participants.

We hope these views are helpful and if you wish to discuss them further please contact Steve Rose on 01793 892068 or myself on 01793 893983.

Yours sincerely,

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