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**Gas Distribution Price Control Review - Fourth Consultation Document**

Dear Joanna,

RWE npower welcomes the opportunity to comment on Ofgem's Fourth Consultation on the Gas Distribution Price Control Review (GDPCR) and does so on behalf of all its licensed gas supply and shipping businesses.

This consultation focuses mainly on the initial analysis by Ofgem's consultants of each GDN's operating, capital and replacement expenditure requirements along with Ofgem's methodology for determining certain financial issues. As we are not party to the detail of the analysis from Ofgem's consultants and do not see it as our role to comment on financial issues relating to GDNs our response is limited to making high level comments on some of the issues raised in the consultation. We did however, welcome the opportunity to participate in Ofgem's recent seminar regarding this fourth consultation and found it useful in aiding our understanding of the issues concerned.

We support Ofgem's proposed treatment of related party margins in relation to xoserve and connections margins. In the event Ofgem were to adopt a core services plus User pays model for xoserve financing, which we strongly advise against, it may be necessary to reconsider the issue of xoserve margins. However, the extent to which xoserve's costs will be funded directly by shippers or through price control will be hard to gauge under this model and so determining those elements of costs on which a margin should be chargeable will be difficult.

With regard to non-operational capex, whilst we can see some merit in treating this as opex from an efficiency and consistency perspective we would be concerned about the P0 impact this could have based on GDNs current forecasts for non-operational capex. A level of non-operational capex equivalent to 25% of GDNs total capex requirements appears, on the face of it, to be excessive. However, if this is deemed to be efficient we would not wish to see this fully expensed without some form of mitigation measures being taken to reduce the P0 impact.

The analysis of GDNs direct opex costs by Ofgem's consultants seems to imply they have assumed that GDNs will lose 55% of their existing meter work over the next price control period (see paragraph 3.22). If this is what is implied we believe this is

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a gross exaggeration, and whilst Ofgem may have ambitions that their metering strategy will deliver competition resulting in significant and speedy reductions in incumbents market share this optimism is not shared by the majority of the supply community. Retaining this assumption is likely to overstate the amount of revenue GDNs are allowed for emergency work and in our opinion this apparent assumption should be revised downwards.

Ofgem's analysis of the volume driver suggests that the original assumptions on which this was based may have been flawed and that based on their current analysis of those GDN costs which are throughput related there could be a case for removing the volume driver altogether. Whilst this may be the case, the effect of the volume driver is to broadly align allowable revenue with the current methodology for collecting transportation revenue from customers. We would not wish to see the volume driver removed therefore without fully understanding the methodology by which GDNs will charge customers going forward. Any removal of the volume driver is also likely to reduce the risks GDNs are exposed to which should result in a commensurate reduction in their cost of capital.

We are not convinced that a revenue driver based on either capacity, customer numbers or connections would necessarily improve the efficiency by which allowed revenue is adjusted to reflect actual costs incurred, and so do not see merit in pursuing this further.

Whilst we support, in principle, the use of rolling incentives, we believe Ofgem are best placed to judge the merits, or otherwise, of applying capex, information quality, opex and repex incentive mechanisms in the next price control. We have no strong opinion therefore on whether it is appropriate to strengthen the capex rolling incentive but would expect Ofgem to carefully consider the trade offs that might result and the extent to which this might lead to GDNs cutting necessary capex, or earning inappropriate returns.

Such judgements, and the design of any incentives, should draw from their experience of previous price controls and the current electricity distribution price control. In the event incentive mechanisms are put in place, information should be made publicly available on GDNs performance against these incentives annually.

Finally, following recent decisions on Modification Proposals 90 and 116, GDNs should now be in a position to update their forecasts of the costs they are likely to incur in implementing the enduring offtake arrangements and managing their networks on an ongoing basis in accordance with the new regime. Our understanding is that with the exception of implementation costs associated with Modification Proposal 116 GDNs will be allowed to recover these costs (to the extent they are efficiently incurred) through their price control. Once these forecasts have been made available we would expect Ofgem to subject them to the same degree of scrutiny and scepticism as was applied to shipper costs. We would also expect Ofgem to be vigilant in assessing any systems solutions GDNs propose for implementation of Mod 90 as the those currently being floated at the UK Link Committee would seem to us to represent an over elaboration.

We hope our comments above will help to further inform your thinking on relevant GDPCR issues. Should you wish to discuss them in more detail please do not hesitate to contact me.

Yours sincerely,

Steve Rose
Economic Regulation

Sent by e-mail and therefore not signed