

RWE npower



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**Transmission Price Control Review – Gas Entry Baseline Re-consultation
October 2007**

Dear Bob,

We welcome the opportunity to comment on the issues raised in this consultation document. This response is provided on behalf of the RWE group of companies, including RWE Npower plc and RWE Trading GmbH.

The level and allocation of baseline entry capacity set out under the Transmission Price Control Review (TPCR) Final Proposals has raised considerable industry concerns. These concerns relate principally to the scale of the changes in baseline levels and the disproportionate and unexpected impact at certain entry points, such as Teesside.

The recent National Grid Gas NTS (NGG) workshops have been helpful in explaining the modelling and analysis that underpinned the determination of baselines and added the transparency that was lacking during the TPCR. The analysis from NGG indicates that there are a large number of alternative ways of allocating the total aggregate baseline as well as in setting the aggregate baseline itself. That there are a number of equally legitimate outcomes increases the sense that there is arbitrariness in the proposed baselines and that the allocation process that has created winners and losers. This is unacceptable and the process for setting baselines must remove these concerns as far as is practicable by placing greater emphasis on the previous baseline that applied at each ASEP and the previous baseline levels as a whole.

An additional concern is that Ofgem only identified narrow objectives for the baseline setting process that seemed to have been focused on their issues with the previous regime and we question whether these were universally shared by actual users of the system. These narrow objectives constrained the outcome of the process at the expense of regulatory stability. This seems to us to completely undermine the objective of strengthening

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investment signals to NGG, as it makes shippers reluctant to commit long-term. Furthermore, it undermines investment decisions taken under the reasonable expectation of incremental rather than fundamental regime reform. We therefore welcome continued debate and further information provision in this area and would like to see a widely agreed methodology as the key output from this consultation process. This should be developed within a framework that includes other objectives such as minimisation of change and regulatory stability and results in equitable treatment across all entry points.

6. We agree with the need to undertake an Impact Assessment, particularly in respect of the buy back risk associated with any revised baselines, and the industry needs to be fully informed in order to make a meaningful input. The consultation document sets out a range of issues to be covered by the Impact Assessment and these appear to be a comprehensive list.

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,

Charles Ruffell
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CONSULTATION QUESTIONS

Chapter 4: TPCR approach to baseline determination

Question 1: Do you agree with the objectives of the TPCR baseline review?

The chosen objectives were not unreasonable but were too narrowly defined. This forced a fundamentally different approach to setting the parameters in the entry capacity regime from those in place from 2002 to 2007. An overriding objective ought to be minimisation of regulatory uncertainty.

Question 2: Do you agree with the modelling approach we asked NGG NTS to carry out? If not, why not.

On balance the high-level modelling approach seems reasonably robust and we do recognise that it is intrinsically difficult to model the network and that there will be an element of subjectivity in the assumptions made. However, modelling assumptions, such as the pattern of flows to meet the peak day and the choice of entry points that are adjusted under supply substitution scenarios, are key determinants of the outcome. It has been demonstrated that different assumptions will lead to different outcomes and creates differential impacts between shippers at the various terminals. It is therefore vitally important that any assumptions are widely understood and agreed.

Question 3: One of the main difficulties we faced in the run up to Final Proposals was to account for zonal constraints. Are there any better ways accounting for zonal constraints?

The extent and location of zonal constraints in the future is not clear to us, given specific NTS reinforcement projects and the change in flow patterns from north-south to predominantly east-west.

Question 4: Are there any other issues we should have considered in this chapter?

Much was made of the fact that the baselines were one part of the overall TPCR package. What has never fully explained was the sensitivity between baselines and buy-back risk, and this needs to be better understood in order to assess changes to both the level and allocation of baselines.

Chapter 5: Sensitivity analysis

Question 1: Would you consider any of the alternative approaches for allocating the free increment as discussed in this chapter more or less appropriate than the approach adopted for the TPCR Final Proposals baselines, please given reasons why.

Our concern here is that we remain to be convinced that either that the absolute level of baseline capacity is "correct" or that it has been allocated correctly. Both of these concerns influence the level of free increment that then has to be allocated. As presented at the recent workstreams, there are a number of equally valid ways that the free increment could be allocated and these should be explored alongside the buy-back implications.

Question 2: We allocated the Caythorpe and Blyborough (Welton) free increments to Hornsea and Theddlethorpe respectively, do you agree with this approach or should these free increments have been allocated in a different way and if so, how and why?

This allocation appears to be arbitrary, rather than rule-based and equally convincing arguments could be put forward for allocating additional capacity to, say, Teesside.

Question 3: NGG NTS presented three principles in order to allocated baseline capacity, namely to (i) allocate in line with physical capability; (ii) constrain not to exceed previous obligated levels; and (iii) broadly commensurate with buyback target. Do you agree with these principles? Please explain why or why not.

See response to question 1, chapter 4 above.

Question 4: NGG NTS presented slightly different ways of reallocating entry capacity to different entry points, would you find these approaches more or less appropriate? Please give reasons why.

These approaches should be considered alongside any equally valid alternative approaches that might be raised during the consultation.

Question 5: Are there any other considerations which we have not highlighted which we should have taken into account?

We think that the latest available auction information should be used as these reflect commitments made given users' current understanding of the regime. Had the extent of the proposed changes been known ahead of the 2006 auctions, there may have been a different outcome at those auctions.

Chapter 6: Way forward

Question 1: Is our approach for allocating the free increment, taking zonal constraints into account appropriate given the premise that baselines need to reflect the physical capability of the system?

As discussed above, we require a more detailed understanding of constraints to make a meaningful response here.

Question 2: Are there any other factors that we have not considered which should be assessed in considering an appropriate adjustment to baselines?

We expect that a number of alternative approaches will emerge as part of the consultation responses and, where credible, these should be assessed. Also, wider objectives such as minimisation of change and regulatory stability should be included, as it must be recognised that parties made investment decisions based on the existing baselines.

Question 3: What are your views on the different options outlined for allocating capacity in a different way, whilst maintaining aggregate baselines at the current TPCR Final Proposals level of 7629 GWh/d?

The case for maintaining baselines at the current TPCR Final Proposals level of 7629 GWh/d has not been made and it may be appropriate to increase the aggregate baseline. This can only be properly assessed if the relationship with buy-back exposure is better understood.

Question 4: What are the advantages and disadvantages of keeping baselines unchanged at their current TPCR Final Proposals level?

The only advantage is that it obviates the need to reopen the price control settlement. The disadvantages include undermining industry confidence and potentially stifling investment and innovation.

Question 5: If we were to increase the aggregate baselines how could we quantify possible increases in buyback costs and/or capex allowance also given the timescales involved?

It is for NGG to provide the analysis. It seems a reasonable assumption that they should already have suitable models available as this risk assessment forms part of their capacity release decision making process.

Question 6: If we were to increase the aggregate baselines how should we allocate the additional capacity? Which mechanism, if any, should we use?

A robust, widely agreed mechanism should be agreed as part of this re-consultation process.

Question 7: Are there any other considerations which we have not highlighted which should be taken into account if we were to increase aggregate baselines?

We accept that the TPCR baselines are part of the wider TPCR package and if the aggregate level of entry capacity baselines were increased there would be an impact on other parts of the package, most notably buyback allowance and/or capex allowance. Furthermore, they are a key input in the current transportation charging model. However, these factors should not be used to prevent necessary changes being made to the baselines.