Ian Marlee
Director, Trading Arrangements
Ofgem
9 Millbank
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27 March 2009

Dear Ian,

National Grid Electricity Transmission and National Grid Gas System Operator Incentives from 1 April 2009 - Final Proposals Consultation.

EDF Energy welcomes the opportunity to comment on the final proposals for the electricity and gas transmission system operator schemes for NGET and NGG to apply from 1st April 2009. Our key comments are covered below, with specific answers to the consultation questions in the attached appendix.

We have always, and still do, support longer term SO incentives scheme generally, since otherwise, particularly with an upside sharing factor of say, for the electricity side, only 25%, any actions requiring capital commitment need a four-fold payback within 1 year for NGET to be financially viable. Our concern is that some smaller capital investments fall between TPCR and this incentives scheme but could contribute to the effective and efficient operation of the transmission network.

We welcome the overall downwards adjustment of the Incentivised Balancing Cost (IBC) target from the initial forecast of £991m to £616m, which has included the implementation of the new Net Imbalance Adjustment (NIA). As stated in our response to the initial proposals, we believe the new NIA better reflects the costs of resolving imbalance. However, while we welcome the reduction from the initial forecast, we feel that the overall incentivised imbalance cost target is still too high. Moreover a relatively low upside cap means that NGET could cease to be incentivised if it became apparent that the figure out turned below £540m.

If you have any queries on this response, please do not hesitate to contact me direct, or my colleague Paul Mott on 020 3126 2314.

Yours sincerely

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Appendix

Chapter Two

Question 1: – Do you consider that the final proposals for the SO incentive scheme to apply to NGET's external SO costs represent a fair balance of risk and reward?

Given that commodity costs have been declining compared to the inevitably slightly "over-egged" forecast that NGET made for this year in their input to Ofgem's earlier, December consultation, the revised target in this incentive mechanism represents a more realistic scheme, though we would still support a lower target which is consistent with the objective of the price control.

Question 2 – Do you consider that the proposed licence modifications appropriately reflect the final proposals as described in this chapter?

We are assuming that the licence conditions reflect these proposals, though they are complex legal instruments which are difficult to understand intuitively.

Chapter Three

Question 1: Do you consider that the final proposals for the SO incentive schemes to apply to NGG's external SO costs represent a fair balance of risk and reward?

We generally believe the set of final proposals that Ofgem has set out following industry consultation represents a fairer balance of NGG's risk and reward, except for the environmental incentive, which is overly generous compared to other industry sectors.

NTS Shrinkage

- As previously stated it is difficult to verify NGG's shrinkage volume forecasts but the lower target level of 142GWh seems more appropriate. We note that Milford Haven and Teesside flows are difficult to predict. However, as more LNG supplies will be brought to the UK, we welcome Ofgem's and NGG's views on how this should be catered for in accurately calculating and minimising shrinkage volumes; simply removing them from the equation to minimise NGG's risk does not seem appropriate or sensible in the long-term.

- We still believe that the scheme for shrinkage should be an annual scheme rather than a multi-year scheme lasting 3 years; all respondents also supported single-year in the previous consultation. However, we would be willing to support a longer 3 year scheme where there is evidence that a longer term incentive scheme could create additional efficiencies and cost savings. More information on how NGG intends to efficiently decrease its shrinkage volumes would be welcomed.

- Regarding UAG we agree with Ofgem's final proposals to make it a 3 year scheme until the end of this price control rather than a 5 year scheme. However, we do not agree with the asymmetrical sharing factors and seek clarity on why Ofgem has not stayed with the original 50/50% split.

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Operating Margins

- We agree that holding costs associated with operating margins should be passed through for this year only and that NGG should remain incentivised on the utilisation element.

Residual Balancing

- We agree with and welcome Ofgem's proposals to tighten the Linepack Measure (LM) incentive to ensure NGG does not enter the market and get rewarded unnecessarily. We also agree that lowering the LM maximum payout will place greater emphasis on the price measure.

Information

- We welcome Ofgem's decision to reduce NGG's demand forecasting target from 3.5% to 3% with the incentive lasting only one year.

Environmental

- As stated in our original response to NGG we believe the EU ETS price was a more appropriate reference price to use over the Defra carbon shadow price, which is a social carbon price. This would also put NGG on a level playing field with other industrial sectors for this type of industrial processes. Ofgem's support for Option A creates an over-generous incentive for NGG compared with other industrial sectors.

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