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Dear Hannah,

The length of the price control period

The Wales & West Utilities (WWU) response to the “Current thinking working paper on the Length of the price control period” is set out below.

WWU is a licensed Gas Distribution Network (GDN) providing Gas Transportation services for all major shippers in the UK. We cover $\frac{1}{6}$ th of the UK land mass and deliver to over 2.4 million supply points. WWU Limited is one of only two Licence Operators that focus solely on Gas Distribution in the UK.

WWU has been fully supportive of the Ofgem review of the Regulatory framework known as RPI-X@20. We have, and will continue to support the workshops and consultation processes as it is imperative that any conclusions implemented are workable and result in an improved regulatory framework.

It is quite clear that the current challenges facing the UK and UK energy are different to the challenges that existed twenty years ago when the RPI-X regime was introduced. The UK energy market structure, the application of the RPI-X regime, and Licence Obligations for the different participants have also evolved significantly over that time.

There are many current uncertainties in the UK and the UK energy sector. Whilst we have known legislation for our environmental challenges, there is clear uncertainty and ambiguity about how and when the UK will meet these challenges. This leads to an uncertain energy mix from 2020 to 2050. If you couple this uncertain future with the current economic climate and growing fuel poverty in the UK, it appears to suggest the need for a regulatory regime that is flexible and one that evolves to address the changing environment.

It is recognised throughout the world that the UK RPI-X@20 basis of network regulation has proven adaptable and has served the energy sector well. We believe the existing RPI-X regime with some enhancement, as proposed through the RPI-X@20 emerging thinking can facilitate the outcomes desired by all.

Against this background and context we think extending the length of the price control period for Gas distribution is one aspect of the emerging thinking that has not been proven to better

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

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facilitate the desired outcomes. We have a concern that an 8 year review period could add further uncertainty and risk.

Evidence for change: The straw man proposes an 8 year review period but we do not think there is any evidence that an eight year review period would result in a better regulatory outcome.

Uncertainty: A five year control period in itself presents a number of areas of uncertainty and we feel that an 8 year control period would broaden the scope of these areas. This is further confirmed by the proposed inclusion of more ‘uncertainty mechanisms’ in the extended price control period. In this current climate of economic uncertainty, it could be argued that a longer period of review may result in a greater risk of shocks that had not been foreseen at the start of the review and therefore not identified in the uncertainty mechanisms.

Additional Risk: An 8 year review period could expose energy networks to a greater risk of uncertain financeability. Investors place significant reliance on regular price control reviews and the review of regulatory obligations associated with each control period. A lengthening of the price control period may raise concerns with investors with regard to perceived market risk and may result in a higher overall cost of capital for energy networks.

Political risk: A longer period of review would not only increase the risk that energy networks face as a result of economic uncertainty but also the risks posed by political uncertainty. Although the recent changes in Government have yet to result in significant amendments to the energy policy, it is clear that the future structure of the UK government is far from certain. Future changes in Government and energy policy could result in the need for the price control review to be re-opened at some point in the future and significant changes made to reflect the changes in policy.

Complexity: The potential for small-scale reviews and possible changes in required outputs along with the ‘uncertainty mechanisms’ proposed, would increase the complexity of the regulatory regime already faced by the energy networks. It would also result in an administrative burden on the networks which may undermine any efficiency incentive and objectives that the longer control period is aiming to achieve.

Charging Volatility: We also believe that any increased volatility caused by annual adjustments and small-scale reviews would not be supported by Shippers.

Evolution not revolution: The current UK energy regulatory regime is regarded as best practice around the world which a view supported by a leading credit agency in a recent publication. An extension to an 8 year regime for Gas Distribution may be seen as a “revolutionary change” and lead a perception of increased regulatory risk. Any major changes to the well established, highly regarded regime should only be undertaken where clear improvements to the regulatory framework can be demonstrated.

Mini Reviews: The straw man proposals indicate possible “mini reviews” where significant divergence from Outputs emerges. It is our understanding that Output delivery is clearly linked to cost and enabling projects. Therefore if a material divergence from Outputs emerges, it is likely to facilitate new discussions about enabling projects and hence funding. Therefore the existing shorter five year control period could in fact be more sustainable for the delivery of Outputs. Distribution Networks currently have the option to ask for five year price control review final proposals to be referred to the Competition Commission. It is



unclear what equitable remedy would be available to a Distribution Network if it was not satisfied with the outcome of the year 4 "mini review".

We hope our continued engagement and comments help facilitate an improved regulatory outcome and help the RPI-X@20 team.

Yours sincerely

A handwritten signature in black ink, appearing to read "S. Edwards", with a long, sweeping underline.

Steve Edwards
Head of Commercial and Regulation
Wales & West Utilities