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Dear Anna

National Grid's Response to Ofgem's Decision on values within the stakeholder satisfaction output arrangements (electricity transmission licence special condition 3D and gas transporter's licence special condition 2C)

Thank you for the opportunity to respond to the consultation on the proposed licence modifications to National Grid's transporter and electricity licences, which seek to implement Ofgem's decision on the values for the stakeholder satisfaction output arrangements for both licences as well as additional housekeeping amendments to National Grid Electricity Transmission's licence. This response is on behalf of both National Grid Gas Transmission (NGG) and National Grid Electricity Transmission (NGET). It is not a confidential response.

We believe the decision and the proposed licence modifications to exclude the stakeholder satisfaction component of the incentive from years 1 to 3 through the application of a weighting of 70:0 in favour of customer satisfaction is inappropriate for the following reasons:

- the policy decision set out in Final Proposals is to encourage transmission owners to be more outwardly focused and responsive to changing stakeholder needs. The policy is implemented through a financial incentive mechanism described in Final Proposals and incorporated into the existing licences, which provides for a penalty or reward of up to +/- 1% of the transmission owner's annual revenue; and
- throughout the consultation processes and, indeed, in this final consultation on Ofgem's decision it is expressly stated that the incentive is to be a penalty or reward of up to +/- 1% and this was enshrined in the NGET and NGG licences through paragraphs 3D.11 and 2C.11;

yet the effect of the decision and proposed licence modifications delivers an incentive of only +/- 0.7% of annual revenue for years 1 to 3 of the RIIO Price Control. The overriding principle that the incentive should comprise a penalty or reward of up to +/- 1% of annual revenue is front and centre of all the informal and formal consultations. It is, however, only in the most recent decision that

there is a move away from this overriding principle. This approach undermines the principles of a transparent price control and does not promote regulatory confidence.

We recognise that Ofgem may have concerns that by adopting a weighting of 100:0 that this may have the effect of over amplifying the impact of our performance in relation to the customer element of the incentive. Ofgem is also clear that after considerable thought and taking account of stakeholder responses that they consider the customer element of the incentive should remain constant over the RIIO period at 70%. Further, that a 30% weighting for the stakeholder element of the incentive is "...warranted because of the relative importance of this aspect of wider stakeholders...". Finally, Ofgem are clearly of the view that 70:30 is the correct long term weighting that should apply to the incentive. Given all this, it is not clear to us why a weighting ratio of 70:30 is not the appropriate position for the entire RIIO-T1 period. A 70:30 weighting would ensure that the intentions set out in final proposals are met (the weightings add up to 100%), it avoids any increased weighting to customer in the first 3 years of RIIO-T1, and it provides reward for our performance against Ofgem's target for the stakeholder satisfaction element that Ofgem have now said going forward is the baseline against which performance should be assessed.

We accept Ofgem's decision on the proposed targets and weightings for years 4-8. We also accept Ofgem's decision on the proposed targets for years 1 to 3. We would, however, invite Ofgem to reconsider its decision in relation to the weightings of the stakeholder satisfaction and customer satisfaction components of the decision for both the electricity transmission and gas transporter licences for years 1 to 3 of the price control and to modify the licence to reflect the policy intent and aims set out in Ofgem's decision.

If you require any further information, or if you have any questions regarding this issue, please contact Andy Balkwill in the first instance on 01926655988 or at andy.balkwill@nationalgrid.com

Yours sincerely

[By e-mail]

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