



Mr Stuart Easterbrook
Transmission Charging Manager
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Dear Mr Easterbrook,

GB Transmission Charging: Revised Proposals Consultation

Thank you for the opportunity to respond on this subject again. The comments made in my previous responses still stand.

Although these proposals reduce the tariff disturbance to customers and suppliers they still leave a 25 % increase in an unhedgeable regulated third party charges. We regard this as unacceptable for a number of reasons.

In this response we raise issues of:

1. Impacts of tariff instability on market efficiency
2. Differential Anti-competitive effects of short notice changes
3. Materiality of the effects on SME sector suppliers
4. Materiality of the effects on standalone suppliers (without generation)
5. Impact on the efficiency of the wider economy

The creation of artificial volatility in an unhedgeable element of costs will give rise to the creation of a risk premia that will be paid by customers. The cost of which needs to be offset against the market improvements in market efficiency of immediately implementing a new cost reflective methodology. These assessments need to be made over the 40 year asset lives of network investments and customer investments. In addition, the unhedgeable nature of these charges will stifle product innovation in the market.

We do not believe that the step changes in charges created by applying full cost reflectivity immediately is justifiable when the costs of the risks are taken into account. We believe that a phased implementation should reduce the risk premia and therefore produce an overall more efficient market.

The proposed tariff disturbance has an anti-competitive effect in that it differentially affects different types of suppliers. The impact of these proposals is greatest on the standalone Suppliers of SME customers due to the underlying nature of contracts in this sector.

The six largest suppliers all have a significant volume of domestic customers, any change in charges may contractually be immediately passed onto these customers. They also have significant generation that will benefit from the proposals, therefore the net effect of the changes on their overall businesses will be minimal or even slightly positive.

Parties who solely supply the SME sector with no generation are therefore discriminated against by these proposals in favour of the larger vertically integrated players. We believe that the anti-competitive effects are disproportionate to the benefits gained by having a step change in charges by having fully cost

reflectivity implemented on day 1. We therefore believe that a phased approach to implementation would be justified to mitigate this adverse impact.

Companies plan the operation of their businesses in a financially prudent manner. They do not budget for windfall gains and only have a limited budget for unforeseen costs. Most would prefer to have a minimal budget for unforeseen costs and windfall as this makes for inefficient use of working capital. Customers are therefore likely be willing to give up the windfall gains in order to avoid the unforeseen costs as this would lead to an operational increase in the financial efficiency of their businesses.

Tariff disturbances due to a cost reflective based approach are unpredictable, as cost reflectivity is an art not a science and differing economists will produce different results. There is therefore a potential for significant tariff disturbance as different individuals decide on what cost reflective actually means.

In the context of the current proposals, in order to achieve hold demand side tariffs constant the D/G split would need to be 58:42. If the maximum rate of change of transmission costs was set at 5% per annum, then it would take 5 years to achieve the proposed position, this is a pragmatic solution that minimises customer disturbance, allows suppliers and customers to plan in a sensible manner their businesses and allows them to optimise the use of their own working capital. This will improve the overall effectiveness and efficiency of the wider economy.

Regards

Keith Munday
Commercial Director