Pricing Managers
Gas Distribution Networks

04 November 2008

Dear Gas Distribution Networks

EDF Energy Response to Distribution Networks Pricing Consultation Paper DNPC04: "Methodology for Determining the Balance of Revenue Recovery between LDZ System Charges and Customer Charges".

EDF Energy welcomes the opportunity to respond to this consultation; we support implementation of this proposal.

EDF Energy would also like to take the opportunity to commend the GDNs on the work that has been done and the information provided within this consultation to aid responses. In particular the information provided on how costs are incurred and treated within the appendix has allowed us to judge whether this proposal will ensure that costs are correctly targeted. In addition the provision of expected net impact on charges for customer load bands has also been helpful in identifying the impact that this proposal will have on the different market sectors. From our perspective, whilst this net impact is useful, it would have been more beneficial to have a detailed breakdown of the impact on specific charges as this allows us to identify the specific impacts on load bands using our pricing assumptions and ensure that there are no unexpected or unintended impacts on different classes of consumers within the load bands. We would therefore like to thank Northern Gas Networks, National Grid Distribution and Wales and West Utilities for their prompt response to our information request for this information which enabled us to undertake a detailed analysis of the impacts for these networks.

From the information provided in the appendix, it would appear that the proposed allocation of costs between LDZ System and Customer Charges is appropriate and the proposed change to the split would ensure that costs are correctly targeted at those who are causing them to be incurred on the system. In addition correctly targeting of costs at Shippers, will be beneficial to competition by ensuring that there is not a cross subsidy between market sectors. It would also appear that this proposed change will ensure that changes in the Transportation Business since 2003 are reflected in appropriate charges.

Finally EDF Energy would note that issues have been raised with the impact that this proposal would have on iGTs and their Relative Price Controls (RPCs). EDF Energy understands that total charges will increase for legacy arrangements, and that the profit margins that iGTs make from customers not on legacy arrangements will be impacted. However given the wording of Standard Licence Condition A5, we are unsure whether these impacts are within the scope of this consultation. It would appear that the issues raised with

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this proposal are in fact issues with how the RPCs are set. Given the increasing size of the iGTs, EDF Energy would question why there is not a specific price control for this sector?

In relation to the specific questions posed within the consultation EDF Energy would make the following comments:

Question 1: Should the charging methodology be changed so that the balance between LDZ System and Customer Charges for each DN is based upon a network-specific estimate of the split of relevant costs?
EDF Energy believes that the balance between LDZ System and Customer charges should be based upon network specific estimates of the relevant costs. In particular we would note that the GDNs already develop network specific charges, and Shippers and Suppliers have to have systems and processes in place to support these. The introduction of network specific splits, and so network specific charges should therefore not pose an issue for Shippers and Suppliers. In addition we would note that Licence Condition A5.5 requires the Licensee to develop a charging methodology that is cost reflective. Network specific splits would be seen to facilitate this objective.

Question 2: Should the DNs rebalance the LDZ System and Customer Charge each time the level of charges is changed or should the DNs rebalance the LDZ System and Customer Charges only if the forecast revenue split deviates from the cost reflective target split by more than a set threshold value, if so the DNs would welcome feedback as to whether the threshold should be set at +/- 1%, or 2% or at another level.
EDF Energy supported the introduction of modification proposal 0186 on the grounds that it provided Shippers with predictability of where distribution charges were going. From a Shipper's perspective it is the predictability of charges that is of paramount importance, with stable charges being a secondary issue, as this allows us to ensure that any future changes are incorporated into our pricing strategy. Updating the rebalance every time that charges are changed would detract from this predictability, especially as the main driver for this appears to be driven by the AQ review and associated impacts on SOQ, which the GDNs have limited visibility of. In addition only rebalancing the charges when a set threshold was breached would also detract from this predictability, as Shippers and Transporters would be required to guess when this threshold breach would take place in the future.

EDF Energy therefore believes that these charges should be rebalanced every 5 years. This could coincide with the start of a new price control, when the GDNs are required to report their costs to Ofgem, or with the re-setting of Seasonal Normal Demand which EDF Energy understands has a significant impact on AQs and SOQs. This would provide Shippers and consumers with predictability over their future charges, whilst also helping to ensure that charges are cost reflective. We would also note that given Standard Licence Condition A5, the GDNs would still be required to ensure that there charges are cost reflective and so they would be able to re-balance their charges if there was a significant divergence from the proposed split. We would expect this divergence to be at least 3% as there will be a cost associated with incorporating this change into Shipper's pricing structure. We believe that this will ensure that charges are as cost reflective as possible, whilst also promoting competition by providing certainty to Shippers of when any re-balancing would occur. We would however note that all of the options would require the Transporters to publish an annual update of the current split to provide some visibility and predictability around the charges. We would suggest that this would be best accommodated through the mod 186 report.

Question 3: Is there any reason why the proposal should not be implemented from 1st April 2009?

As noted in our response to DNPC03 Shippers generally require a significant lead time to incorporate any changes in charges into their pricing structures. For EDF Energy the cost of changing our retail tariffs is significant. These costs included system updates, publication costs, staff training and mail shots to impacted customers. We therefore aim to limit the number of retail tariff changes in a year and will only make changes in response to a combination of factors, including changes in Transportation charges. This explains why we place such an emphasis on the predictability of charges, and why we require sufficient lead time to incorporate regulatory changes such as DNPC03 and DNPC04 should they be implemented.

In addition I&C contracts tend to be either bundled (with Transportation and energy costs included in a fixed rate) or with Transportation costs pass through. These contracts generally tend to be for 12 month periods, with a very limited ability for Shippers to adjust their rates within these contracts. For bundled contracts we generally require a minimum of a 12 month notice period to ensure that any changes are incorporated into these contracts, again explaining our emphasis on predictability of charges. The risk to EDF Energy of having insufficient notice period is that we are tied into a contract with our I&C customers at a loss, due to an unexpected change to a Transportation Charge. As a preference we therefore believe that this change should not be implemented until 1 April 2010, and all methodology changes are accompanied with a 12 month notice period.

I hope you find these comments useful, however please contact my colleague Stefan Leedham (Stefan.leedham@edfenergy.com, 0203 126 2312) if you wish to discuss this response further.

Yours sincerely

Seb Eyre

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