

To all interested industry parties

Anne Bennett
Charging & Revenue Manager

anne.bennett@uk.ngrid.com
Direct tel +44 (0)1926 653445

www.nationalgrid.com

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Dear Industry Colleagues,

Forecast of TNUoS tariffs from 2012/13 to 2016/17

When the GB Transmission Network Use of System charging methodology was approved by the Authority in March 2005 it attached six conditions to its approval¹. Condition 5 sought to facilitate competition within the electricity supply industry and required National Grid to:

“publish information at least once a year on the forecast future (at least five years) path of tariffs under a range of credible generation and demand scenarios (consistent with those already contained in the Seven Year Statement) as soon as practicable, and no later than April 2006”

Since the introduction of this condition, National Grid has prepared such a forecast in an annual Information Paper² around the time when tariffs are set, the most recent published in January 2011. The forecast is based on the Seven Year Statement (SYS) and includes information about the locational and non-locational tariffs over a five year period; an explanation of the drivers for the main year-on-year tariff changes; and a sensitivity analysis. This involves the construction of a charging model for each year and numerous separate models to understand the individual events (be it changes in generation connections or network investments) that drive the trends.

National Grid believes that there is merit in providing a forecast of future tariffs and, based on feedback from customers, the forecast has evolved to help ensure it is continued benefit to the industry. The report is of greatest benefit where the final published tariffs are in line with the forecasts that have been made in previous years. Our ability to prepare an accurate (and therefore meaningful) forecast is dependent on several factors and, in particular, on having an agreed methodology upon which tariffs can be calculated.

¹ NGC's proposed GB electricity transmission use of system charging methodology - The Authority's decisions (March 2005) <http://www.ofgem.gov.uk/Networks/Trans/Archive/ElecTrans/BETTA/Publications/Documents/1/10033-8005.pdf>

² Condition 5 – Long Term Tariff Publication <http://www.nationalgrid.com/uk/Electricity/Charges/gbchargingapprovalconditions/5/>

Whilst the charging methodology is subject to change, the nature and timing of such changes has historically limited the level of methodology uncertainty at the time when the forecast and supporting analysis is being prepared. This year, however, the precise nature of the enduring TNUoS charging methodology is currently unclear due to Project TransmiT, the ongoing review of transmission charging.

Under Project TransmiT, two high-level alternative approaches to charging alongside the status quo are being considered in addition to the existing arrangements. Whilst Ofgem have indicated their initial view of the best way forward³, to date the remaining two options have not been ruled out. Once Ofgem have published their final recommendations in spring 2012, the precise details of any revised methodology will still be dependent on a CUSC modification. Given the standard timescales associated with the CUSC modification process, National Grid does not expect the final arrangements to be confirmed before autumn 2012. This timetable means there is currently considerable uncertainty in the enduring charging methodology which will affect the quality of any forecasts made for future years.

In order to understand and compare the impact of the different approaches being considered, Ofgem commissioned Redpoint to model future tariffs using the various alternative methodologies⁴. Redpoint's analysis includes a high level of detail on tariffs and the underlying generation and network changes underpinning these. In this light, National Grid is concerned if it were to prepare its own tariff forecast based on the current methodology and/or our interpretation of the various alternative methodologies (none of which are firm and therefore subject to change) we may either repeat work already undertaken by Redpoint, or, in the extreme, prepare information that could prove confusing or misleading if for any reason these are inconsistent. To illustrate this, in theory there could be up to six forecasts covering the same time period, based on differing assumptions of each methodology and the underlying transport model data (where applicable).

Against this background, National Grid has considered a number of options for the most appropriate way to prepare a forecast for the period from 2012/13 to 2016/17. These were outlined at the November Transmission Methodologies Forum (TCMF). Based on discussions at TCMF and following further reflection, National Grid's initial view is that limited additional benefit is obtained through National Grid preparing similar analysis of TNUoS tariffs of each possible charging methodology over the five year period concerned. Instead, we believe that it would be better to delay publishing a full information paper and any associated data until Ofgem concludes the SCR process, when there will be more certainty of the methodology that will apply. However, in the interim, National Grid would look to publish a narrative of the changes driving the tariffs reported in Redpoint's analysis, to assist interested parties in understanding the impact Project TransmiT will have on them, where possible highlighting any major drivers for tariff changes in each of the five years.

In summary, National Grid believes that the approach outlined above will provide greater benefit to interested parties than other options available because:

³ Project TransmiT - Electricity transmission charging: assessment of options for change
<http://www.ofgem.gov.uk/Networks/Trans/PT/Documents1/Project%20TransmiT%20Dec11.pdf>

⁴ Modelling the Impact of Transmission Charging Options – A report by Redpoint Energy
<http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=174&refer=Networks/Trans/PT>

- i) the provision of the Project TransmiT narrative will help interested parties to understand the impact on their businesses;
- ii) potential duplication of the Redpoint analysis of the future trend of TNUoS tariffs under each possible charging methodology considered by Project TransmiT is avoided; and
- iii) an updated forecast of tariffs will be provided in the form of an information paper once a clear view of the ongoing TNUoS charging methodology is established.

Comments and views are invited from interested parties on each of the issues raised in this letter and National Grid's proposed solution. Following receipt of comments, National Grid will publish its conclusions on the approach to be undertaken, at the end of January 2012, subject to any discussions required with Ofgem to seek confirmation that the intended approach will satisfy the relating charging approval condition.

If you wish to provide comments on the contents of this letter, responses are welcome via email to wayne.mullins@uk.ngrid.com. To ensure that your comments and views are considered by National Grid in its conclusion, responses must be received by close of business on Wednesday 25 January 2012.

Yours Sincerely

Anne Bennett
Charging and Revenue Manager