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Dear Craig,

**Regarding the application of the Transmission Network Use of System charging methodology for determining generation charging zones for the price control period beginning 2007/8**

Thank you for the opportunity to respond to the above consultation. E.ON UK believes that the present zoning criteria are appropriate, but would support some limited changes to improve the process.

In the light of the present transmission price control review, we believe that it is a sensible time for National Grid to assess whether or not the present zoning criteria are appropriate. We believe that when setting the generation zones National Grid has to balance two important objectives.

- The first of these objectives is cost reflectivity. Charges must reflect the different costs which are imposed on the system depending on generators' decisions on where to locate their plant. Moreover, charges must year on year be responsive to changes in the distribution of generation and demand on the transmission network.
- The second objective is stability. In order to provide an appropriate environment for investment in generation, charges should not be subject to significant degrees of change year on year.

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Clearly, these objectives conflict with each other to a certain extent. At one extreme, if charges are fixed year on year, then cost reflectivity is compromised as they cannot reflect any changes in generation or demand on the network. The aim is to achieve the appropriate balance between the two which maximises the benefit in terms of efficient investment and operation of the network, as well as promoting effective competition in generation and supply.

Our analysis tends to suggest that the most significant changes in TNUoS charges occur, in respect of individual connections, when there is a change to the zones or when there is a change in the basis of the charging methodology, which of course normally results in a change of zones as well. At other times, year on year price changes are less volatile, but do react to changes in the pattern of generation and demand on the system. We believe that the present balance between stability and cost reflectivity is about right. However, there are a couple of areas which could be improved.

- At present, there is provision for zones to be reviewed between price controls, if a significant change should occur which justifies it. We believe that this should be used extremely sparingly, such as when a connection with a high level of cabling justifies a new zone for that connection alone. We would prefer to see clear criteria under which such an early rezoning exercise would be considered.
- The present zoning criteria include a requirement that zones should be set such that no individual nodal charge in the zone is more than +/- £1/kW from the zone average. This is a nominal value which hasn't changed for some time. It may be worth considering whether this should now be adjusted for inflation.

We do not consider that it is necessary to ensure that the zoning criteria are met through the whole period between price controls. We note the thirty zones which may be required in order for this to be achieved for the forthcoming price control period. This level of granularity is excessive and is likely to mean that there will be a great deal of volatility in charges year on year, as the smoothing effect of the zones would be largely lost.

We believe that it would be preferable to undertake the rezoning exercise using the present criteria and ensuring that the number of zones is maintained at a reasonable level. Indeed, there appears to be no reason why the number of zones should change from present levels. This may change in the future however, in a similar way to the increase in zones which occurred at the beginning of BETTA, when new offshore TOs are incorporated into the system. As these circumstances would result in the extension of the geographical area covered by the transmission system, it would appear appropriate to increase the number of zones accordingly.

We do not however believe that there should be an objective to maintain the geographical boundaries of the existing zones. Whilst we believe that it would be sensible to maintain a similar number of zones, the boundaries of these zones must be allowed to move to reflect changes in the distribution of generation and demand on the transmission system.

Therefore, in summary we would support.

- Changes to boundaries only when a new price control is implemented.
- A review of the +/- £1 zoning criteria to ascertain whether it is appropriate to adjust for inflation.
- The aim of maintaining a similar number of zones as at present, with the proviso that extension of the network may require an increase in zones.
- Utilisation of data which is current at the time of the price control change.

This we believe will achieve the correct balance of cost reflectivity and stability in order to promote effective competition in generation and supply.

I hope the above comments prove helpful.

Yours sincerely

Paul Jones  
Trading Arrangements