

Stuart Cook  
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Governance  
Ofgem  
9 Millbank  
London SW1P 3GE

17<sup>th</sup> November, 2010

Dear Stuart,

**Re: Project TransmiT – A Call for Evidence**

Centrica is pleased to be able to provide input to this project being undertaken by Ofgem and is happy to commit to playing an active role in the process going forward. This non confidential response is submitted on behalf of the Centrica Group of companies excluding Centrica Storage Ltd. The response comprises this letter and the attached paper with appendices.

**Context of Project TransmiT**

Centrica is a major user of the gas and electricity transmission networks both as generator/producer and shipper/supplier. This means that the charges play a key role in our business, not only in terms of how they feed through into customer contracts and over what timescales, but also as regards our investments in power generation. Given that total transmission charges are in excess of £0.5bn per annum for Centrica (excluding CSL), this impact is extremely significant and a key exposure for our business.

The essential backdrop to all the initiatives and reviews currently underway is the bigger picture of energy policy objectives – i.e. the provision of secure, sustainable low carbon energy supplies, to meet the needs of present and future consumers, at reasonable cost.

The single most important policy driver is low carbon generation, which requires massive investment in generation as well as anticipatory capex in electricity transmission, and the physical requirements associated with increasing cross-border interconnection and market coupling. When taken in conjunction with the natural cycle of network asset renewal it is clear that the industry is facing investment demands on a scale not seen since the original electrification of Britain.

In gas, the expected development is less dramatic, but the principal investment driver will be long term supply security as the UKCS continues to decline, leading to increased requirements for storage and alternative supplies such as LNG imports. The unpredictable mix of imported gas flows and the likely growing need for highly flexible gas generation to

back up intermittent wind may also require network reinforcement to improve capacity flexibility.

Given the number of wider policy initiatives currently underway, we would also note the interactions of TransmiT with the EMR, RIIO-T1 & RIIO-GD1 and Ofgem's Significant Code Review on electricity cashout as well as the importance in ensuring that the subsequent outturns of these are aligned with each other.

### **Taking forward TransmiT**

In taking forward TransmiT, we believe that there are important requirements that need to be considered in terms of what is needed from a transmission charging regime. There should be a simple, overarching objective - to promote the delivery of sustainable and secure energy to present and future customers, at reasonable cost. To do this robustly, the regime will need to: create incentives for efficiency; encourage appropriate investment and give locational signals to new resources; be technology neutral and facilitate security of supply.

To underpin this objective and associated requirements, we believe that the principles of better regulation should be applied, namely that outputs should be transparent, accountable, proportionate, consistent and targeted. In the context of TransmiT, we believe this should mean the application of 7 core principles: cost reflectivity, sustainability, alignment of incentives, technology neutrality, predictability, transparency and avoidance of undue complexity.

### **Centrica's position**

Centrica believes that overall, measured against what we believe to be the right benchmarks, the existing regimes are generally fit for purpose. Nevertheless, there are clearly issues, some of which have resulted from previous bolt-on fixes to the current regime, that need to be addressed:

- Issues inherent in extending the onshore transmission charging regime offshore and the perverse outcomes that result
- Improvements in transparency and predictability of transmission network and system charging
- Securitisation of capacity requirements in both gas and power
- Lack of cost reflectivity resulting from the current gas entry charging regime
- The anomalies in the electricity charging regime resulting from interconnector charging policy
- The application of NTS charges to gas delivered directly into distribution networks
- Setting out clearly where issues will be resolved, for example, Canatxx and the NTS credit issue, if the conclusion is that they are not to be in scope for TransmiT

And some areas where we believe material change is not needed:

- We continue to support the principle of locational signals to drive efficient siting of investment
- Where generation reduces the need for investment, then this "service" should be rewarded. Hence we support the principle of the benefits associated with being exemptible and embedded, but accept that additional work may be needed (for example in the area of transparency of flows) to ensure this is sustainable in an era of higher levels of embedded generation

We recognise that this response is not exhaustive and that given the uncertainties mentioned in the context section, in particular, EMR and RIIO, the scope of TransmiT cannot be restricted solely to issues from this call for evidence. It must be flexible enough to address further issues arising during the review period, which may be significant.

### **Outputs and next steps**

In summary, in addition to the points raised above and in the body of this paper, we believe that there are four further outputs required from project TransmiT:

1. A reasoned view about expectations for change in the context of constraints/wider environment
2. Clarity about what the regime should be delivering
3. A clear set of criteria against which any proposed changes can be assessed
4. A viable set of possible reforms

In order to maximise its effectiveness and quality of output, TransmiT will need to base its work on an agreed vision of how the wider energy environment is expected to develop due to policy changes, especially where this will obviously lead to significant changes from the status quo. To do this, the review will need to reflect the development and outcomes of the other reviews. We believe that this would include the increase in low carbon/clean generation, infrastructure investment to support CCS, growth in offshore generation, wind intermittency issues and consequent changes in the location of generation as ageing coal and oil plant closes and is replaced by wind, nuclear and other technologies. Other important issues will be the development of smart grids with the associated issues around electric vehicles, alternative heat sources and increased demand side participation.

To support the evidence based approach, there should then be a robust impact analysis as to how all these changes will impact on the transmission system and the charging arrangements (for example, wind intermittency could dramatically increase BSUoS charges), so that the proposed new regime can be tested to see that it is fit for purpose for the next 15 years.

The main focus of this response has been providing our views on points 1-3 outlined above. Going forward over the course of the review period, we will be engaging with Ofgem and DECC as well as with industry colleagues through consultations, stakeholder events and industry discussions to provide answers to the final point, developing a viable set of reforms. However, in order to best enable us to do this, we would ask Ofgem to provide stakeholders with a list of objectives and guiding principles and a more detailed plan of the process for project engagement. Given its unique position and the importance of transmission regimes to the company, we believe that Centrica is well placed to work with Ofgem as a key stakeholder as this project develops.

If there are any of the points raised in this response that you would like to discuss in more detail, either Ricky Hill (07789 579169) or I would be happy to help.

Yours sincerely,

*By e-mail*

Alison Russell  
Senior Regulation Manager, Upstream Energy