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Dear Stuart,

Project TransmiT: A Call for Evidence

International Power plc (IPR) is responding to your call for evidence on behalf of its operating subsidiaries in the UK: First Hydro Company, Saltend Cogeneration Company Ltd, Rugeley Power Ltd, Deeside Power Ltd, Indian Queens Power Ltd., and IPM Energy Retail Ltd.

We welcome the opportunity to comment on the issues raised, and agree that it is timely to review the current charging arrangements in the context of the evolving challenges faced by industry.

Review Objectives

We agree with the sentiment of the stated objectives, however they are very high level and therefore imply an overly broad scope for this review. Following this Call for Evidence process it would be useful for Ofgem to narrow down to some specific outcomes and objectives in order to minimise any uncertainty for market participants. Ofgem will be aware that with a number of other live reviews under way (including DECC's market reform programme) there is a risk of investment hiatus which may be prolonged in the event that the nature of transmission charging (a key component of generation economics) remains in doubt.

Principles for current charges

We believe that the current principles employed in setting charges do indeed remain largely fit for purpose. In particular it is as important as ever that transmission charges should be set such that they provide good value for customers whilst being mindful of the need to develop a safe and secure transmission system. This means that cost-reflectivity should remain central to these principles in order to retain efficiencies and promote effective competition.

For instance, we believe that TNUoS tariffs should be reflective of the costs of providing transmission and as such encourage generation to site at appropriate locations. It is important that a new generator, when considering where to locate, should be faced with the associated cost of transmission. The relative cost of a high resource, high transmission cost area compared to a low resource, low cost transmission area should be fed through to the developer in the form of differential transmission charges. This will ensure the developer considers the cost of transmission in its economic decision on where to site.

Continuing to apply differential TNUoS charges will thus deliver best value for customers. We believe that a flat or "postage stamp" charge would potentially unwind this benefit to the customer as it does not provide the necessary cost signals.

We note the increasing relevance of Ofgem's sustainable development duties, and recognise that relatively high TNUoS tariffs in areas of high wind resource may appear counter to the desire to expand wind capacity in these areas. However, TNUoS charges form only one element of project economics and it is important to retain some independence of charging methodologies from energy policies on individual technologies.

Potential improvements to current arrangements

Notwithstanding our general agreement to the current principles, the changing nature of our market does indicate that there may be some modifications to the current arrangements that would be desirable to better meet these principles.

- We believe that there is benefit in examining the detail of the existing methodology to consider whether it can be improved. The existing methodology views all plant in an identical form irrespective of their physical characteristics: for example, wind, tidal and pumped storage plant all have physical characteristics that lead to a reduced need for transmission. The current ICRP model charges all of these plant types at the same level. We believe that there may be merit in establishing a technical working group led by National Grid, to review the operation of the current ICRP model with a view to designing a methodology that moves away from peak based ICRP charging, concentrating on the potential of 'probabilistic' charging. This would mirror work currently being undertaken in the SQSS review to examine more closely the transmission investment requirements associated with different technologies.

- Energy market arrangements are designed around financially firm connections with balancing mechanism bids typically used to reduce generation in constrained areas.. However, physical disconnection as result of a transmission fault or intertrip operation is treated differently, resulting in only partial compensation based on a refund of TNUoS charges (after the first 24 hours). As the probability of disconnection is a function of the Transmission Owner's network investment decisions (based on the SQSS), different generating stations have different probabilities of suffering a disconnection event despite potentially paying the same zonal TNUoS charge. Overall this means that where a generator is potentially more "vulnerable" to disconnection due to local network configuration, the current compensation arrangements would tend to be wholly inadequate. We believe that this should be addressed by reviewing the financial arrangements for disconnection with a view to applying the same methodology as is used for constraints. This would lead to a more efficient

transmission system with the cost of transmission being balanced against the probability of constraints or disconnection, with all stations being treated equitably.

- It would also be expedient to review the security factor used in the ICRP model. The actual level of security varies by location and therefore in many circumstances the commonly applied security factor does not reflect the level of security that is enjoyed by an individual generator.

- Whilst we believe that a location based differential charge is appropriate we believe that there would be merit in considering if the net revenue collected from generation should be set to zero ("G=0"). It is the differential cost not the absolute cost that is important in location decision-making. This would ensure that the GB market increases harmonisation with the rest of the EU, and will equitably reduce barriers to investment.

- Embedded generation can have a significant effect on the quantity of transmission that needs to be built in a given area. Currently embedded and transmission connected generation are subject to different charging arrangements but the effect in transmission terms can be identical. We believe embedded generation above a de minimis level [say 5 MW] should be subject to the same charges as transmission connected generation where the effect on transmission is the same. We accept that there are legacy issues related to existing generation where deep connection costs have been paid, and it would be inappropriate to subject some embedded generation projects to charges without a refund of capital contributions and/or reasonable transitional provisions.

Process

Given the background to gas charging and the recent work on an enduring exit regime we cannot see any benefit in considering gas related arrangements any further under this review. We do not anticipate there to be benefits in, for instance, trying to harmonise arrangements with electricity in any way.

We note the potential role of the SCR process in this review. There may be merit in pursuing any potential code changes via this route however we need to be mindful of the timescales involved. If significant changes are identified this may unduly prolong uncertainty.

On a related issue, charging arrangements are due to be incorporated into industry codes shortly and given the timing and potential scope of this review it may be necessary to ensure that there is a moratorium on related modifications until further certainty is provided via the TransmiT process.

We hope you find the points made in this response useful and would be pleased to provide any additional details if this would be helpful.

Yours sincerely,

Simon Lord
Transmission Services Manager