

3 October 2003

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BETTA Project
Ofgem
9 Millbank
London
SW1P 3GE

GCHPL-B100-10

Dear David

Fortum Group, owner of Grangemouth CHP Ltd, welcomes the opportunity to respond to this consultation paper. We have included our responses to Parts 1 and 2 of the paper in the same letter, since the two responses cross-refer.

August 2003 Consultation Paper: Transmission Charging under BETTA – Part 1

Responsibility for Charging Methodologies

We note Ofgem's assessment set out in paragraph 5.6 of the paper, in favour of giving GBSO responsibility for development of charging methodologies and charging statements. In principle we concur with this reasoning and therefore support Ofgem's proposals. However, we are aware of the complexity of the "behind the scenes" arrangements to be covered by the STC and, should expedience in this area favour a structure whereby TO's created their own methodologies and statements subject to requirements for consistency, we would not see that as significantly compromising BETTA's objectives.

Licence Obligations

We support continuation of the current framework for the regulation of charges based on licence obligations, and regulatory oversight.

We support the use of a mode based around NGC's existing supplementary Standard Conditions. However, we believe that the existing Conditions applying to NGC should be more widely reviewed than has been set out in the current consultation paper, in order to establish whether they require revision prior to the implementation of BETTA. We note that the consultation paper identifies two areas where changes are likely: so that the conditions work under the new circumstances of a GBSO and two TOs; and to address discrimination issues arising from those circumstances. We believe that the existing conditions will require modification to address both these issues; we have not included detailed comments in this response but would be in a position to provide those if required.

We have identified a third area of concern which could be addressed, amongst other means, via the Licence Conditions. We set out below our concerns that the existing England and Wales transmission charging methodologies, if extended to a GB basis, might have a number of undesirable or discriminatory effects. Since the existing England and Wales methodologies have been developed under the existing NGC Licence Conditions it follows that, in order for the methodologies to be different for GB charging, either the Licence Conditions will have to be different, or the interpretation of those conditions would have to recognise the changed circumstances in moving from the England and Wales system to the GB system. As a general principle, we would favour a licensing framework which reflected the required outcome, rather than relying on downstream decisions and therefore we believe that Condition C7A should be amended.

Basis of consultation

We note that the existing England and Wales arrangements and methodologies have been taken as the starting point for consultation. Whilst this provides one starting point, our view is that the eventual GB methodology will have to be substantially different to that currently employed in England and Wales, so basing the consultation process around an inappropriate model will increase the time required and / or reduce the effectiveness of the consultation steps proposed.

Process and Timetable

We welcome the proposal of a process which endeavours to give market participants a reasonable period of time to consider the proposed amendments to the charges. However, we have reservations regarding three aspects of the proposed process.

- The process outlined, whereby the licence conditions will be developed by Ofgem / DTI after which responsibility passes to the initial GBSO for developing methodologies and charging statements which are consistent with those licence conditions, is in our view somewhat too mechanistic given the possible implications of the introduction of GB transmission charging. The choice of transmission charging methodology could have a profound effect on current and future market participants throughout GB and particularly in Scotland. It is our view that the direct effects on participants, and the consequences of those, should be clearly identified and decisions should be taken on how to handle them at a policy level by Ofgem / DTI, rather than passing a set of licence conditions to the initial GBSO and then waiting to see what arises from the process – at which time the scope for Ofgem / DTI to play a role in achieving a balanced overall policy will be diminished.
- The process as set out could result in the initial GBSO beginning a consultation process on charging methodologies in November 2003 before Ofgem/DTI's consultation on licence conditions has been issued in December 2003. In the absence of a steer on possible changes to licence conditions, or some other guidance as to how the existing England and Wales conditions might be applied to a GB system, we would anticipate that NGC would have to consult on methodologies which are close to the existing England and Wales methodologies, even though a different set of conditions might actually be more appropriate.

- We feel that the consultation process proposed to be followed by the initial GBSO might achieve a more robust result if an additional formal cycle of consultation was introduced. The current process of initial thoughts in November 2003, initial proposals in March 2004 and final proposals in October 2004 would be adequate if the methodologies were anticipated as evolving only slightly and incrementally from the existing England and Wales ones. If, however, any more substantial variation was to be considered, we would anticipate this would be introduced only in March 2004 (in response to comments following the November 2003 initial thoughts). In that event, an additional formal cycle of consultation would provide transmission users with an opportunity to explore the consequences of revised proposals rather than moving straight to final proposals.

Pattern of Cost Recovery

We support the broad principle that GB users should pay for the GB system with cost-reflective and non-discriminatory cost recovery on a GB-wide basis rather than sub-divided within GB. However, we have concerns regarding the choice of methodology for establishing cost-reflective charges, for both practical reasons and because of the underlying principles.

In practical terms, we note that a “trends continued” application of the existing use of system charging methodology to Scotland will result in a sharp reduction in UoS charging for consumption and a four to six-fold increase in charges for generation. Changes of this magnitude, especially against a historic background of stable UoS charging regulation and increasing transmission system cost efficiency in Scotland, are likely to leave generation assets in Scotland stranded by virtue of UoS charging far in excess of that provided for in their financing. Should the more fundamental issues not be addressed as we suggest below, we would wish to see some form of transitional arrangements over timescales which reflect realistic asset lives which shield peripheral generation and demand from step-changes in charges which their financing could not support.

We see this practical side-effect, and the wider issues relating to renewables covered under Part 2 of the consultation, as a symptom of the shortcomings of the existing England and Wales charging methodology, rather than a shortcoming in the overall objective of GB-wide cost-reflective charging. We note that the current methodologies have been judged to be consistent with the licence conditions in the context of the England and Wales system. However, we maintain that the current methodology is not the only one which could be said to be cost-reflective, and in fact contains shortcomings which – whilst apparently tolerable in an England and Wales context – render it discriminatory in the context of the GB system. Those shortcomings have their origins in basing the charges at a particular zone on the incremental cost of the next capacity to be connected at the zone, rather than on the cost of the capacity already connected. One consequence of the particular methodology which has been chosen is the creation of unrealistically sharp locational signals at nodes towards the periphery of the system. Whilst we support the principles, we would wish to see a more cost-reflective and less discriminatory charging methodology (possible candidates do exist), and should that be best achieved by amending licence objectives then we would wish to see those licence objectives amended as part of the BETTA project.

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We agree that locational pricing is likely to result in transmission charges higher in Scotland than in some other areas. However, as we set out above, we do not believe that the current methodology, which results in relatively sharp locational pricing signals, is a suitable one to be applied in a GB context. Should a more suitable transmission charging methodology be selected, then the impact on peripheral generation or demand of any type, including renewables generation, would be lessened. In the context of the other support measures for renewables technologies, a more moderate transmission charging methodology would be less likely to disadvantage renewables generation significantly.

We have reservations about the implications for transparent, non-discriminatory and cost-reflective charging arrangements of the creation of sub-classes of location and / or technology which would qualify for differential treatment. With changing circumstances, there would be a significant risk that re-classification of a technology or area could result in step-changes in transmission charges faced by generation and demand located both in the affected area and further afield. In the longer term, as the balance of renewables generation on the system increases, the implications of such factors would increase very significantly.

General Comments

We would welcome early publication of any form of programme which sets out the way the BETTA project is anticipated to develop, to facilitate planning of resources and to provide context to the consultation process.

We would be happy to expand on our views should that be required.

Yours sincerely

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Asset Manager