TRANSMISSION PRICE CONTROL REVIEW

RESPONSE TO CONSULTATION DOCUMENT, DECEMBER 2005

WARWICK ENERGY LIMITED

Warwick Energy Limited (WEL) is a developer of UK energy projects including conventional and renewable power generation schemes and gas storage schemes. WEL is therefore interested in the general development of the UK's transmission systems for both the gas and the power sectors and has recent experience of trying to bring new capacity onto both systems.

In our experience there are considerable deficiencies in both the current gas industry arrangements and the electricity industry system, particularly since the introduction of clustering. We would hope that neither structure is adopted for the period from 2007 for either sector as neither is proving flexible enough to cope with the current environment nor do they allow sufficient strategic investment to occur to ensure adequate security of supply for end consumers.

The Consultation report identifies increased planning uncertainties that have become evident since the last TPCR although the list in Section 3.5 seems to ignore the additional role that new and proposed Interconnectors (both gas and power) will play in increasing these uncertainties. The Interconnectors are clearly a very welcome addition to the gas and power transmission systems but modelling their effects is tricky to say the least. They can switch from import to export role (or 'do nothing' mode) on a daily (or even within-day) basis.

This last year has shown that the simple assumption that high UK demand would see all facilities importing at or near maximum capacity has been proved false for the gas and power Interconnectors (and the LNG terminals).

WEL recognises that modelling future system flows, especially over such long periods, is a very difficult and complex challenge. The number of uncertainties, particularly on the supply side, is very significant over the coming years and some reasonable changes to certain assumptions can dramatically change the outcomes from the models. It is therefore difficult to have much faith in the outcome of any such modelling at the moment even if we were in agreement with some of the base assumptions made – which, in many cases, we are not.

The fundamental changes that will occur in the UK Gas Market over the next few years will alter the way that various parts of the system are used. In many cases however the extent of the changes are difficult to predict. WEL believes that neither the baseline flow assumptions nor the auction signals are accurate or sufficient to provide a picture of future usage patterns with any confidence. Alternative, interim, planning assumptions, using multiple scenario analysis, must be made until the new flow patterns appear.

As an example, WEL does not agree with the assumptions that the new import terminals will be utilised as predicted, as supplies (whether they be LNG, Norwegian or Russian supply sources) will often be directed, sometimes at short notice, to other international markets with higher price signals.

NG should be encouraged and allowed to invest in the gas and power transmission systems to facilitate all of the reasonably expected variations in flow patterns to cope with the new range of entry combinations. The cost of this 'deep' system workload cost should be recoverable from end users (as the beneficiaries of the resultant increased security of supply). Both current gas and power arrangements (using different methods) attempt to allocate some or all of these costs to new capacity and this often inhibits the very projects that the UK needs to encourage.

New entry capacity for both gas and power should continue to be made to pay for the 'shallow' reinforcement that is specifically needed to allow that project to gain access to the transmission system. All other costs should be smeared into system charges. The end consumer will ultimately pay for this new investment in all cases (either directly or indirectly) but the current, flawed gas modelling work and the new Clustering approach for power creates artificial barriers to entry for much needed capacity.

The entry of the UK into a global gas market should raise Security of Supply issues much further up Ofgem's agenda. Consideration must be given to encouraging and supporting new investments, such as storage projects, that will help satisfy domestic demand and reduce price volatility.

Gas Storage

WEL believes that the current Ofgem policy of treating all new NTS connections in the same way is wrong. The real cost implications for the flexibility needed to support interconnector operations is underestimated and the benefits of gas storage schemes are ignored.

The various benefits of storage schemes should be recognised and any system costs involved should be smeared across system users who will benefit from the additional security, reduction in volatility and lower prices that will result. WEL believes that all gas storage schemes should have a zero entry cost as a maximum and that negative entry prices, as used in the UK power sector, should be considered to encourage new storage capacity further and to reflect, even in a crude way, the benefits that these schemes provide to NG and all gas users. The current system allocates significant notional costs to such projects, inhibiting their development.

The additional flexibility offered by new storage facilities will help to dampen price volatility, to the benefit of both NGG and consumers, and will also normally act in a supportive way to help NGG balance their system at least cost. The current system allows NGG to benefit from their reduced balancing activities (and costs), in both summer and winter, for free.

Another area where Storage is a special case is the lifetime over which it is reasonable to assume that any costs should be recovered. The 10 year period currently assumed in UCA calculations is possibly not unreasonable for normal entry points, where contracts and field depletion durations are of this order, but storage projects are designed for much longer lifespans. Recovery of entry costs should be assumed over a 25 to 40 year period to avoid an over-recovery by NGG over the project life.

The biggest error however in the current modelling assumptions used by Ofgem and NGG is the load absorption assumption rather than using the more logical load substitution model. The current methodology artificially increases system load to balance any new proposed entry capacity. This results in a signal for notional reinforcement work leading to higher UCA's which inhibits new capacity. Correcting this mistake on its own will significantly improve the system for the gas network.

Electrical Connections

The recent RETS Revisited Report supports some of the comments made earlier in this note – that regulatory approval should be given to more central spend on the transmission network and that a more coordinated strategic approach is required.

Warwick would particularly like to point out that the move to Clustering, adopted mid-term in the current TPCR period to tackle a particular problem in Scotland, has had a severe negative impact on new projects. The issue of onerous FSL's for new power projects was already a problem in parts of the Country where insufficient transmission investment has been made. The Clustering arrangements add to these problems and involve further complexities and uncertainties.

Deep reinforcement requirements to support a number of new and existing projects should form part of a central transmission spend and not be allocated (and then reallocated) onto new projects.

Other Specific Responses to selected Questions

6.15 Warwick agrees with Ofgems conclusions that the charging methodologies model should be separate from the price control to provide more flexibility.

6.19 The focus on 'user commitment' is now outdated for systems that now face significant changes and uncertainties and that consumers must now face a modest increase in direct costs to ensure their long term security of supply.

7.117 Whatever decision is made on entry arrangements we do not support the need for offtake reform. The case has not been sufficiently made for the need and the cost and complexities involved are yet another burden that the industry could do without in this period of change.