The Office of Gas & Electricity Markets

Memo

To: AARODG Members

From: David Hunt

Date: 27th March 2006

AARODG – 3rd meeting, 23rd March 2006

Attendees

Colin Sausman (chair), Mark Copley, David Hunt, Sundeep Klair (Ofgem), Adam Brown, Nick Pittarello (NGET), David Densley (SSE), Jim McOmish (SPT), Danielle Lane (Centrica), Robert Langdon (Airtricity), Richard Ford (BWEA), Terry Ballard (RWE Npower), John Capener (British Energy), Malcolm Taylor (AEP), Rupert Judson (EDF Energy), Paul Jones (E.On), Mike Davies (Wind Energy)

Apologies

Keith Miller (Teeside Power), Simon Lord (First Hydro), Mark Petterson (Warwick Energy)

Introductory discussion

The group discussed the options detailed in the paper produced by Ofgem in relation to access building block 2.

Option 1 – status quo: MT noted that under this approach there was no guarantee there would not be a change to BSUoS, and the status quo may involve higher or lower user charges.

Option 2 – allow all parties to connect: the group noted that in this approach constraint costs are likely to be substantially higher than at present. JM noted that in this approach there are still likely to be planning lag issues, and that National Grid will still be required to invest against the planning standards. RF stated that changing the planning standards could be explored as an option. JM reminded the group that the SQSS retains an economic test to justify investment. Some members of the group considered that the economic test may be one-sided.

Option 3 – allow all parties to connect subject to consents: RF clarified that the intent of BWEA's connect and manage approach was that allowing all parties to connect would be subject to local works. JM suggested this should be subject to local landowner

agreement and way leaves. The group considered that there were several issues with consents, and that we shouldn't be too prescriptive, rather just recognising the issues. Another approach in option 3 was to consider consents plus a period. MT suggested that one trigger could be upon receiving financial close. The two extremes associated with option 3 are access based on a time period or access based on a trigger plus a time period.

Option 4 – allow connection in planning plus X years: this was moved into the discussions of option 3 as a variant.

Option 5 – allow parties to apply for short term products once CEC is secured: this is similar to the status quo, and the group decided to move it into option 1.

Option 6 – develop less firm products: NP noted that there are issues with terminology associated with 'less firm' products. The Group discussed the meaning of non or less firm access. There was agreement that such a product would differ from those currently available in two aspects. The first relating to the notice period at which access became firm and the second relating to the compensation that would be received in the event that the access could not be delivered..

Option 7 – intertripping arrangements: MT noted that since the implementation of CAP076 there are administered arrangements for system to generator operational intertrips, and there are also commercial intertrips bilaterally negotiated with NGET. At a high level, intertrips can be installed as an alternative to system reinforcement.

Option 8 – greater use of derogations: the group considered that derogations don't necessarily negate the need for capacity. The Group noted that Options 7 and 8 were potentially technical solutions to complement one of the options discussed previously.

Option 9 – portfolio TEC: the group expressed a view that there was no real appetite to explore portfolio TEC in detail, but that it was an option and should be kept live. One member of the group noted that there could be charging implications of adopting a portfolio TEC regime.

NGET presentation on short term access

NGET outlined that the key differences between firm and non-firm products was that there is no compensation if rights are withdrawn. A less-firm right therefore implies a different form of compensation if a firm right is withdrawn. NGET highlighted that there was scope for alternative access products to STTEC and LDTEC in a world of spare capacity, which can broadly be categorised in the form of restrictions to volume, or restrictions to price. One model of limiting volume may be to restrict access to certain times of the day. Another model is to limit volume and cap liabilities with a buy-back price. Where there is no spare capacity, NP considered that there are two models: users purchase rights and GBSO purchases rights.

RF considered that the option of the GBSO buying back rights maps closely to the 'connect and manage' approach. PJ considered that there it was unclear what the aim of purchasing from users was as there are two options: a redistribution of available capacity and an increase in available capacity. The view of the group was that it should really be targeted at the concept of redistributing what's available.

MT considered that describing capacity as a commodity was not strictly accurate. His point was that capacity is a locational concept, which necessitates exchange rates between areas.

E.On presentation

PJ ran through the consequences of accepting a bid as a capacity interruption for the purposes of cash out in a short and long market. The general message was that in both states of the system the overall effect is to raise prices. An alternative to treating the interruption as a bid would be to treat it as system BSAD, and leave it unpriced. However, another view was that there could potentially be an alternative way of treating interruption actions, such that the costs feed through into cash out via priced BSAD. However, as cash out prices are intended to reflect purely energy actions, a curtailment of capacity, which would be for system reasons, should not be priced in cash out.

NGET presentation on usefulness of information generated by user commitment

NGET gave a presentation on why financially firm information on intentions to utilise capacity would be beneficial. These benefits to the end consumer include: better planning information and ability to make more efficient investment decisions, higher purchasing power, equity of rights, information transparency and cost savings.

The group questioned what the scope was to release the off-peak product mentioned in NGET's presentation.

Action – NGET to consider how many MW could be released in the off-peak product identified in the presentation

Action – DD has been considering constraint implications of less firm products and will report back to the group

Returning to discussions of the options in more detail

The group agreed that with the options now crystallised, the focus of the group should be on what access building block 2 should address. Views from the group included addressing the need for better utilisation of existing capacity and removing barriers to entry. With this in mind, the group reconsidered whether the options addressed these issues.

CS outlined that a route to assess the options is to consider how they operate presently, and how they would operate with extra capacity products. One view was that on the basis that TEC is not available, new products can not be used. CS clarified that the issue relates more to whether any access can be acquired prior to transmission reinforcements being built. If you have CEC, you can still get STTEC and LDTEC for consecutive strips, although this approach represents a risky strategy, particularly depending on the delay to acquiring TEC.

MT questioned whether or not there was a product that was superior to LDTEC. MT suggested it would be useful to quantify the usefulness of TEC by assessing what would have happened if LDTEC had existed from April 2005. MD suggested that there are

issues surrounding the bankability of a system where you are conferred non-firm rights, but that these issues could be overcome if a PPA could be devised which includes a defined contracted MWh which can be utilised by a generator over a period of time. JM suggested that the bankability of a project is of paramount importance to a developer. If the terms of the connection offer are undefined, bankability is severely hampered.

Action: NGET to think about what the effects would be of having LDTEC from April 2005, and what other products might be devised

Action: MD and RF to think about bankability and how a PPA contract might be devised

The group considered whether it was possible for NG to make a connection offer that can be turned down at little recompense. On the whole it was thought that this would be difficult. However, MT suggested that a generator has the option of asking for a variation to design standard.

CS suggested that a connect and manage approach would offer a user TEC at the same time as CEC. Some members of the group considered that this might mean that more TEC is required than could be managed, and that SQSS issues may be created. RF considered that the potentially large constraint costs associated with connect and manage could be managed until TEC is delivered. Some members of the group considered that connect and manage was the approach that has been adopted in Scotland. Connect and manage infers additional BSUoS costs, but one view from the group was that additional income from early TEC could be utilised to offset the costs.

Action: RF to think about charging and revenue restriction high level scenarios

In a connection in X years situation world there was some discussion that varying triggers could be used to define X before TEC can be granted. If X is dependent on consents, there may still be uncertainty associated with when you receive TEC. The same applies if the scenario is consents plus X. Some members of the group suggested that this approach and connect and manage were similar, in that in connect and manage, X is zero.

In a world where X is fixed at say 3 years, there is a resulting buy back risk on the TOs, and a late delivery risk with users. With connect and manage, constraint costs are socialised, and apportioned on a different basis to TNUoS. MD noted that there has been a change to the powers of local authorities in relation to wind farm developments.

Action: MD to circulate a note on local authority planning changes

CS asked whether in a world where there is a buy back system, there should be administered prices until wider works are completed. JM noted that in gas buy back costs are full.

In a connection in X years, MD stated that X could vary dramatically. Where X is greater than 5 years, this forces a lapse in the planning standards.

CS asked what value user commitment has to TOs and generators in terms of information provision. DD stated that it was difficult for some to make a longer term

commitment. Moreover, DD noted that the user commitment is simply to pay for capacity, and not necessarily to use it – the latter is most useful to the TOs. RF concurred that there may be limited use of user commitment.

DL questioned whether there was a timing issue with regard to when the commitment is posted. The options are: cash up front, invoice or security deposit.

JM stated that decommissioning can also incur costs as voltage support may need to be maintained. In this situation user commitment information may be useful. However, several members of the group recognised that there is a danger with tying in investment with user commitment information, unless it is credible.

CS asked the group what benefits the generation community would see from user commitment information. One group member suggested that there would be benefit to users arising from TOs making efficient investment decisions on the back of user commitment information. CS considered that an additional benefit was that the information could help to reduce stranding risk. MT suggested that an alternative mechanism of acquiring information on users' intent was to mandate in the Grid Code in OC2. Several members of the group considered that the probability of stranding assets in a highly meshed system were quite low. CS mentioned that stranding risk may increase in extreme locations in GB.

Action: Ofgem to write up discussions on section 3

Action: MT to consider what OC2+ might look like

CS outlined that looking forward, the last meeting would be devoted to the ARODG report. Meeting 4 is intended to discuss the rest of access building block 3, and meeting 5 may be used to pick up additional issues, including interactions with block 1.

Action: Ofgem to begin drafting the ARODG report, reflecting discussions on ABB 2