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Dear Simon,

Potential new System Operator quality of information incentive schemes for National Grid Gas (88/06)

Thank you for the opportunity to comment on your consultation on the incentive scheme for NGG SO for the coming winter period.

We note that the incentives proposed within this consultation are intended for a short duration only, from October 2006 until March 2007. Whilst we agree that it is appropriate to incentivise the performance of the System Operator over the Winter period, we also believe that these incentives can and should form the foundation of a more detailed and focussed arrangement for the longer term.

In this response I will address the specific questions posed in your consultation but in summary we are supportive of the application of incentives to the provision of this key information. We have been concerned for some time at the inaccuracy of the figures published in this context. These items do have a significant impact upon the actions taken by Users in balancing their own portfolio and therefore upon the wider market. We believe that the most appropriate approach is to identify the information which is most relevant to Users' balancing actions, and to publish this in a timely fashion. Rather than identifying a separate information set to the wider community, we believe that it would be more efficient and effective to publish a subset of this information from a common source on the website, within a reasonable period.

Chapter 3 – Benefits to customers of improvements in quality of information provided by NGG

Question 3.1: Do you agree that the scope of potential benefits from improved quality of information is correct?

In general terms there is a naturally a benefit to all recipients and parties relying on information of this nature if the data is reliable in terms of its accuracy and timeliness.

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Information provision which fails to meet these criteria can be unhelpful and at worse, misleading. This could result in inappropriate actions being taken and resultant costs being incurred.

Question 3.2: Do you agree that the potential benefits from improvements in demand forecasting accuracy are quantified appropriately?

We have had significant concerns about the inaccuracies in forecasting experienced for some time. Such errors will inevitably have a direct impact upon the actions necessary for Users to achieve a balance of supply and demand on their portfolio. In addition to the direct impact upon the individual Users, these inaccuracies will affect the market more generally, particularly on days where the supply-demand balance is tight and this will often influence prices. We support your view of the benefits that have been identified in the paper and the manner in which these have been quantified.

Question 3.3: Do you agree that the benefits from potential improvements in website performance are quantified appropriately?

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Although the provision of information on the website is less critical to the effect upon the market as a whole, we concur that the provision of this information does hold direct benefits to those not directly involved in achieving a balance position.

Chapter 4 – Ofgem's initial proposals

Question 4.1: Do you agree with the choice of performance measure for the gas demand forecasting accuracy and website performance incentives?

We are of the view that the performance measure should be more challenging. Whilst we recognise that 100% performance in these areas is probably unachievable, a standard of 5% improvement is likely to be well within reach with minimal effort for a reasonably substantial reward. We believe it would apply a greater incentive if payments were graduated to reflect the effort required. For example, a 5% increase would result in a minimal payment, but a 15 or 20% increase would result in a more substantial payment.

Although we do not have the information to hand, it does occur to us that it may be valuable to compare this performance with a number of previous years, rather than just a single year. To assess the performance and improvement over a number of years would serve as a more reliable reference and should certainly be a feature of the enduring arrangement.

Question 4.2: Do you agree with the proposed scope of both of the proposed incentives?

We recognise that these proposals contain an initial simple scheme that can be introduced for the coming winter. It would not be appropriate to introduce something complex in this timescale, however, we do believe that the subject warrants consideration of greater sophistication in the longer term.

We concur that the accuracy of the forecast at 14.00 day ahead is a key provision as we believe that this forecast is the one most likely to drive the day ahead price and will also improve the quality of forecasts which follow.

Although the accuracy of total system demand is of some benefit to Users, a focus upon subsets does carry much greater value. With a total system incentive, the result could be a

much improved forecasts in one area, for example NTS, which allowed the incentive to be paid out but with no improvement in the accuracy in the remainder of demand. Therefore we suggest that a first level of division, which could be in place for this winter, would be to split NTS and DN/LDZ demand, as these two areas will be influenced by different factors. Any further development of subsets is probably best considered in the next phase.

Question 4.3: Do you agree that the incentives should not be weighted towards any specific period within the duration of the incentive?

We are of the view that there is no particular advantage in weighting the incentives toward specific parts of the year at this stage. With the benefit of the experience of this short period of incentives being applied, looking forward, it may be that there is some merit in doing so at a later stage. We do believe that there would be value in focussing the incentives at times of particular system stress, which may arise at any time of year. For example, the identification of days of High, Medium and Low demand (as per Figure 6 in the paper) when a multiplier could be applied to the incentive. This would reward accuracy at times when it proved to be of greatest value.

Question 4.4: Do you consider posting of key data within 20 minutes of real time to be an appropriate measure of timeliness to use in the website performance measure?

As mentioned above, we believe that information provision should be driven by Users' requirements and delivered via the Gemini system. This agreed set of information can then be made available to the wider community via the website. A lead-time of 20 minutes for this provision does seem reasonable. We would draw particular attention to the maintenance of performance levels on the Gemini platform and delivery in this area not being prejudiced by an incentive for wider disclosure.

We believe that there also need to be a measure of the resilience of the website. Particularly at times of system stress, it is likely that the website itself will be subjected to a high hit rate and a failure at such a time would be counter productive to the intent of the provision.

Question 4.5: Do you consider Option 1 or Option 2 of the demand forecasting accuracy incentive to be most appropriate?

Question 4.6: Do you consider Option 1 or Option 2 of the website performance incentive to be most appropriate?

Although we do have some concerns about incentives being applied which do not address deterioration of performance, in the circumstances of this short duration incentive period it may be appropriate to implement a scheme giving an upside only. We would wish this specific issue to be more fully addressed in the longer term.

Question 4.7: Do you agree with the proposed duration of the incentives?

The proposal is to apply these incentives for a very short period only, from October 2006 until March 2007. We recognise that this is only an initial stage in the introduction of a more enduring regime but we believe that there may be merit in applying this initial structure for a full 12-month period as the value of this information may not be limited to the winter months. However, we do concur that the progress and effect of the incentive regime should be kept under review in order to inform any necessary changes and the design and application of the more enduring arrangements.

Question 4.8: Do you agree with the proposed method of recovering any resulting cost from these incentive schemes?

We do not concur with the proposal to simply recover the costs of these incentives from the SO Commodity charge. We would far prefer to see a more focussed allocation of costs. For example, the incentive related specifically to NTS and LDZ forecasting accuracy should be applied to this category of supply points, potentially through charges applying to those supply points.

Summary

We are supportive of the application of incentive arrangements to the provision of this information and its accuracy. We are of the view that this forms only a starting point for the development of such incentives and we would be happy to meet with you to explore ways in which this could be further progressed.

Please contact me if you require any further information.

Yours sincerely,

Mike Young
Commercial Manager