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value for all customers*

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Dear Hëdd,

Fulfilment of conditions attached to the Authority's approval of the GB transmission charging methodologies – GB charging condition 2

On 17 October 2006 National Grid Electricity Transmission ("NGET") submitted to Ofgem a report on GB charging condition 2 entitled "The treatment of intermittent generation in the GB Charging Methodology"¹.

In approving NGET's proposed GB use of system charging methodology in February 2005, the Authority attached five conditions to that approval. Each of those conditions related to future actions to be taken by NGET which the Authority considered might reasonably be expected to promote further the attainment of the relevant objectives.²

The second of these conditions ('charging condition 2') required NGET "to identify, review and assess further the technical basis for a range of alternative methods (including the method adopted in the approved methodology) of estimating, and reflecting in locational charges, the incremental costs of capacity. NGET should consult with interested parties to identify the range of alternative methods to form part of this technical assessment. If the review identifies potential improvements to the existing methodology, NGET should bring forward modification proposals for implementation no later than April 2007. A report on progress shall be published in April 2006. In the event that NGET concludes that there

¹ www.nationalgrid.com/NR/rdonlyres/C2C4143B-3DB3-4D48-97C3-C3B1EC69CB0A/11670/Condition2finalreport.pdf

² The relevant objectives for the use of system charging methodology, as contained in paragraph 5 of standard licence condition C5 of NGET's transmission licence are:

- (a) that compliance with the use of system charging methodology facilitates effective competition in the generation and supply of electricity and (so far as is consistent therewith) facilitates competition in the sale, distribution and purchase of electricity;
- (b) that compliance with the use of system charging methodology results in charges which reflect, as far as is reasonably practicable, the costs incurred by the licensee in its transmission business; and
- (c) that, so far as is consistent with sub-paragraphs (a) and (b), the use of system charging methodology, as far as is reasonably practicable, properly takes account of the developments in transmission licensees' transmission businesses.

are no further improvements, NGET should publish a report setting out the conclusions of the review”.

The motivation for the imposition of this condition was to ensure that the methodology, so far as was practicable, complied with standard licence condition C5 of the electricity transmission licence by resulting in charges that reflect costs.

It is Ofgem’s view that the requirements of charging condition 2 have been met. In reaching that view, we noted that, in developing its proposal NGET:

- ◆ invited views on a range of alternative options at the Transmission Charging Methodologies Forum and the Charging Implementation Steering Group;
- ◆ held two industry tutorials to discuss key aspects of the treatment of the incremental cost of capacity;
- ◆ published a progress report on 2 May 2006 setting out an update on its review;
- ◆ published proposed changes to the Statement of Use of System Charging Methodology designed to improve transparency; and
- ◆ published a final report on 17 October 2006.

Notwithstanding the fact that NGET has met the requirements of charging condition 2, Ofgem notes that standard licence condition C5 of NGET’s licence requires it to keep the use of system charging methodology under review at all times and to make proposals to modify the methodology as required with a view to the methodology better achieving the relevant objectives. Ofgem, therefore, expects that, NGET will continue to consider whether further developments in this area could better facilitate achievement of the relevant objectives.

In the interests of providing transparency to users of the transmission system this letter has today been published on Ofgem’s website.

Yours sincerely,

Robert Hull
Director of Transmission