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Dear Colleagues,

Transmission Access Review (TAR) – Open Letter to Industry

As announced in the Energy White Paper 2007, Ofgem and the Department for Business Enterprise and Regulatory Reform (BERR) are initiating a review of the framework for access to the GB transmission system. We are publishing today the Terms of Reference of the review (please see appendix 1). The review will explore a range of issues associated with the technical, commercial and regulatory arrangements, with the chief aim being to support the delivery of the government's aspiration of 20 percent of electricity supplied by renewable generation by 2020 and any targets that may be agreed at European Union level.

The review is timely as developers are facing increasing difficulty in connecting to the transmission system. The volume of generation wishing to connect to the transmission system is substantial and the time taken to build the required infrastructure means that renewable generation in certain parts of the country is facing severe delays in gaining access. There are areas of the system which are physically constrained as a result of the delay to reinforcement works, which has consequences for network users and consumers who ultimately pay the costs of constraining generation off the system.

However, it is not solely the length of time taken to build transmission infrastructure that is delaying generation from connecting to the system. It is also partly the result of industry rules which do not offer sufficiently flexible, bankable access products to allow developers to commission and operate with a less firm connection offer. Whilst there have been attempts by the industry to find a solution, the problems with the existing regime largely remain. With the government's aspiration of 20 per cent of electricity supplied being from renewable sources and with the majority of this yet to be connected, the issues with transmission access are set to become more pressing over time. The implication for connecting a considerable volume of renewable generation is that not only will more transmission infrastructure need to be built, but existing capacity will need to be used more efficiently.

The scope of the review is broad and will look at the arrangements for planning new grid infrastructure, the technical standards used to determine the need for reinforcements, the operational standards, the scope for innovation in grid operation and infrastructure and the commercial arrangements for access to the grid and system balancing. This longer term work will build on that already in progress via the Short Term Access Governance (STAG) which includes shorter

term work in relation to transmission access and the QB Queue. However, whilst the scope of the review is designed to be broad and not restricted by the existing industry governance arrangements, there are limitations to what the review will look at. The review will not consider planning consents issues as these are being taken forward via the Planning White Paper and Energy White Paper, the management of the GB Queue which is being taken forward by National Grid, nor solutions to grid access currently under development in industry governance bodies.

In terms of deliverables, it is expected that an interim report on TAR will be published in December 2007, setting out recommendations for change, prior to a final report in May 2008. In addition we expect to publish a report in September 2007 on the work undertaken by STAG.

Overall leadership of the project lies with BERR and Ofgem, with day to day work overseen by the Management Committee, jointly chaired by Duarte Figueira (BERR) and Robert Hull (Ofgem). The Management Committee will report to a Supervisory Committee led by Jim Campbell (BERR) and David Gray (Ofgem), which in turn reports to BERR ministers, and the Gas and Electricity Markets Authority (GEMA).

We are committed to engaging with industry on issues being looked at by TAR via a combination of workgroups and consultation documents, and would encourage industry to involve itself in the process. We expect to publish a Call for Evidence setting out key options and seeking initial views on the way forward within the next few weeks. The exact timetable of further stakeholder activities is not yet final, but an indication of timetable of the various reports we will be publishing is provided above. Invitations to attend these workshops will be issued in due course.

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Appendix 1 - Transmission Access Review (TAR) - Terms of Reference

1. Purpose of the Review

1.1 To review the present technical, commercial and regulatory framework for the delivery of new transmission infrastructure and the management of the grid to ensure that they remain fit for purpose as the proportion of renewable generation on the system grows.

2. Objectives of the Review

2.1 The review will set out proposals for changes to the framework which will better support the connection of renewable generation to the grid in the medium and long-term. The review will look ahead to 2020 and consider ways to support the delivery of the government's aspiration of 20% of electricity supplied by renewable generation and any targets that may be agreed at European Union level. These proposals will need to be consistent with the Government's energy policy goals:

- To put the UK on a path to cut our carbon dioxide emissions by some 60% by about 2050, with real progress by 2020;
- To maintain reliable energy supplies;
- To promote competitive energy markets in the UK and beyond, helping to raise the rate of sustainable economic growth and to improve our productivity;
- To ensure that every home is adequately and affordably heated.

2.2 The proposals arising from the review will also recognise the duties of Ofgem as the independent economic energy regulator and its primary duty to protect the interests of electricity and gas consumers. OFGEM also has a duty under the Energy Act 2004 to contribute to sustainable development. The proposals will also be consistent with the Government's better regulation agenda.

3. Background

3.1 In the 2007 Energy White Paper the Government announced a review led by Ofgem and BERR of the framework for connecting renewable generation to the grid. The review will examine the technical, commercial and regulatory arrangements through which new renewable generation is connected to the grid.

3.2 Developers have become increasingly concerned about the difficulties of getting grid access. Projects have been delayed due to connection issues. This is mainly due to the time needed to build new transmission infrastructure which results in parts of the network having physical access constraints, but also due to the industry commercial rules which do not currently offer

sufficiently flexible, bankable access products to allow developers to commission with a less than firm grid connection offer.

3.3 Market participants have worked hard to find solutions within the current framework, but the challenges are likely to grow. It is likely, as projects move through the planning process, that grid connection could become an increasingly important barrier to the deployment of renewable generation.

3.4 The review has been established because in the view of Government and Ofgem the expected changing profile of electricity generation, in particular the increasing proportion of variable renewable generation, means that the current framework will need to change. Meeting the Government's aspiration of 20% of electricity supplied by renewable generation implies connecting c. 20GW of renewable capacity (much of it off-shore and onshore wind). This implies that an increased plant margin could be required if the current high levels of system security are to be maintained. It also implies the need for shared transmission access which will allow more generating capacity to be connected for a given amount of transmission capacity if we are going to meet our targets whilst maintaining security of supply.

4. Scope of the Review

4.1 The review will consider the arrangements for planning new grid infrastructure, the technical standards used to determine the need for reinforcements, the operational standards, the scope for innovation in grid operation and infrastructure and the commercial arrangements for access to the grid and system balancing. There are complex interactions between each of these issues. Whilst the focus of the review will necessarily be on the arrangements for generators wishing to access the transmission system, it should also recognise the offsetting effect from the demand side together with the impact of distributed generation. The review will need to recommend the overall framework that best delivers the connection of renewable generation taking into account the potential for reduced carbon emissions, cost to the consumer and the impact on security of supply.

4.2 Key lines of enquiry are expected to include the following:

a. *Access to the Grid*

4.3 As set out in the Energy White Paper, a programme of work (mainly led by National Grid) is already underway under current industry governance arrangements to deliver improved renewable generation access arrangements in the short term. This will be known as the Short Term Access Governance (STAG) workstream. Ofgem will report on progress in this area in September 2007.

4.4 However, the Government and Ofgem believe that the changing profile of GB generating capacity and constraints in the transmission network implies that, in the longer term, there will be a need to share transmission capacity between different forms of generation.

4.5 The review should consider:

- Appropriate commercial mechanisms for allocating transmission capacity, including sharing transmission capacity, especially where it becomes constrained. The review should consider the options available including connect and manage, capacity allocation methods (including auctions), the place of long and short term trading of transmission access rights and the possible need for a product that allows operation in excess of access rights.
- How transmission access rights should best be defined for the purpose of such proposed commercial mechanisms.
- The findings from Ofgem's analysis of the progress being made to improve access under existing industry governance arrangements (STAG workstream).
- Whether proposed commercial arrangements will support accelerated deployment of renewable generation and provide bankable access arrangements
- Whether proposed commercial arrangements will unduly discriminate between generators, and how they may impact security of supply, competitive energy markets, and economic and efficient network operation.

b. *Delivering and Operating Infrastructure*

4.6 There is a need for significant infrastructure in certain parts of the GB system, to connect new renewable (and other) generation capacity. The review should consider:

- Whether the current basis on which infrastructure is planned and operated will deliver the most timely and efficient outcome, in particular in meeting the challenges of developing infrastructure in more remote locations.
- How to exploit innovative solutions, now and in the future, in order to improve connection opportunities. This may be in the type of infrastructure deployed or the operation of the network e.g. through enhanced control systems.

c. *Incentivising efficient use of transmission capacity*

4.7 The mechanisms for managing constraints need to ensure that the right incentives are in place to connect sufficient generation to meet peak demand without creating incentives to stay connected longer than ordinarily justified by the age of plant, costs of generation etc., thereby blocking transmission capacity that might otherwise be available to newly connecting generation.

4.8 The review should consider:

- The role constraint costs play in the transmission system. Constraint costs partly drive estimates of the level of reinforcements required on the network.
- The extent to which the existing mechanisms for managing constraints through system and energy balancing arrangements remain appropriate in incentivising the timely connection (and disconnection) of generation. This is an important part of the longer term vision of having a flexible system so that when electricity generated from renewable sources is available (e.g. when the wind is blowing) it can efficiently and cost effectively replace electricity from higher carbon forms of generation.

d. Implementation

4.9 The review should identify the implementation route for delivery of its conclusions. This will include a review of relevant industry governance arrangements to ensure that they continue to deliver timely, strategically-driven changes to the framework for access to the grid that are consistent with the evolving UK electricity generation mix.

5. Out of scope

5.1 All the following issues are currently being taken forward. They are out of scope, but will provide important context for the review.

- The planning system. Actions in the Planning White Paper and Energy White Paper are addressing this issue.
- The GB queue of projects. NGET are taking this issue forward.
- Solutions to grid access currently under development in industry governance bodies.

6. Deliverables

6.1 Ofgem will report to GEMA and the Secretary of State for Trade and Industry on the programme of work currently being undertaken under existing industry governance arrangements (STAG workstream) by September 2007.

6.2 The review team will report to the Secretary of State for Trade & Industry and GEMA as follows:

- An interim report on Transmission Access Reform (TAR) by December 2007 setting out progress and identifying any areas where the review believes that changes in primary and secondary legislation may be appropriate.

- A final report by May 2008.