National Grid Electricity Transmission and Gas System Operator Incentives from April 09 – Final Proposals Consultation Comments from AEP[1]

The Association welcomes the opportunity to comment on this document although we appreciate at this stage there is little scope for refinement and it is largely an issue of whether or not National Grid (NG) will accept these final proposals.

The main point we would like to make is in connection with the process leading up to these final proposals. We are generally supportive of NG taking a lead in the development of its incentive schemes. We consider that the consultation process and workshops have worked well. However the fact that Ofgem raised concerns about the forecast outturn constraint costs, as late as mid February 2009 highlights that there is a gap in the process at the point in time where NG 'hands over' its Initial Proposals consultation report to Ofgem. At this time NG's views and those of industry are fairly well understood and transparent, but what is lacking is any understanding of Ofgem's views. These do not become visible to industry until Final Proposals are issued, and by this time there is limited scope for further input by industry.

We believe Ofgem should consider ways in which to signal its initial thoughts to industry, as this would aid understanding and reduce uncertainty over what may form part of the final proposals. This could perhaps take the form of an open letter issued shortly after NG publishes its initial proposals conclusions report. This issue was highlighted this year when NG was assessing tenders for Operating Margins provision. NG had made it clear that it would like to have cost pass through on holding costs this year, and this is a significant change from previous years. Yet Ofgem's views on this were unknown until after NG had made decisions on which tenders were successful. We do however note that Ofgem's letter of 20 February indicated that in future it would be appropriate to pass through additional costs necessary to facilitate a change to the safety case going forward. Indeed, if this approach were adopted then industry would not have been so surprised when Ofgem issued its 16th/17th February letters 'Managing Constraints on the GB Transmission

[1] The Association of Electricity Producers (AEP) represents large, medium and small companies accounting for more than 95 per cent of the UK generating capacity, together with a number of businesses that provide equipment and services to the generating industry. Between them, the members embrace all of the generating technologies used commercially in the UK, from coal, gas and nuclear power, to a wide range of renewable energies.

System'. Quite how an issue with such far reaching consequences was left to be addressed so late in the process is a cause for concern.

Whilst it is not strictly part of this consultation we consider there is an issue concerning the provision of information with respect to incentives. It would be helpful to have target costs, actuals and performance against each incentive published in a single place. The provision of data similar to that reported for power would form an ideal template.

We only have one comment to make on the detail of the gas related proposals. This relates to the residual balancing incentive. We consider that retaining a £30 k collar for a linepack change of 15 mcm (where this was previously 20.4mcm) even with a zero band to 1.5 mcm may not have sufficiently weakened the linepack incentive relative to the price performance measure, and could be said to have strengthened it. As a consequence NG may still undertake fine tuning balancing actions to manage its loss under this incentive even for relatively modest linepack changes.

Given the ongoing urgent changes that have been raised to try and deal with the issue of electricity constraints (CAPs 168, 170 and 171) we have been unable to provide detailed answers to all the questions that you pose in this consultation document. Instead we are limiting our response to some key high level comments.

As can be seen from the responses to the CAP170 consultation, our members are concerned about the level of constraint costs arising from the level of constraint management actions, particularly those associated with the Cheviot boundary, and would have appreciated the opportunity to work with NGET to develop proposals to address the issue. It was clear to our members that a significant level of constraints would be required to complete this work.

Following on from this our members have been extremely disappointed at the lack of transparency by National Grid Electricity Transmission (NGET) in relation to services required and costs and that they did not seek new and more innovative ways of managing these costs over the period of the work. Also, it appears that Ofgem has only as recently as mid February taken an interest in this matter when this issue has been known about for sometime. We would have expected NGET and Ofgem to be much more proactive in this area prior to mid February. Some of our members have pondered whether this lack of action calls into question the competency of NGET and Ofgem in handling the SO Incentive arrangements.

One of the consequences of Ofgem requiring immediate action at this late stage in the process is that it has created uncertainty within the industry and for NGET, which we believe is having a detrimental impact. We have seen a host of (urgent) options for change to the industry arrangements (such as CAP170, B/09, the Procurement Guidelines, GB ECM-18 etc.,) being raised and we are all now in a period of turmoil until these options for change are resolved. It is likely that given the very tight timescales the most appropriate solution may not be identified and we will end up with a suboptimal outcome.

In the meantime we are now approaching the main period of constraints (from April onwards over the summer months) with no new or innovative mechanisms in place to help manage the costs of constraints. Had NGET and Ofgem acted much earlier, when the issue was first known to them, then this would have meant our members (and other stakeholders) could have given full (and detailed) consideration to well developed and appropriate options for change to the industry arrangements. This would have led to such changes to the industry arrangements, as considered appropriate, being implemented from the start of April 2009 rather than, as may turn out to be the case, much later into the 2009/10 charging year (by which time significant costs may well have been incurred). We understand further work on the proposed scheme will now continue. An early indication of the process to be followed, including industry involvement and timescales would be much appreciated.

Finally, in looking at the information set out in the consultation our members have noted that last year (2008/09) was actually an atypical year with, for example, the impact of the Large Combustion Plant Directive, nuclear outages and high power prices. In looking ahead it appears to many of our members that these 2008/09 items could be considered as being 'exceptional' and as such are unlikely to be repeated in the year in question (2009/10). Therefore, in future, these costs should be greatly reduced (irrespective of whether the various options for change to the industry arrangements are implemented) which equates to a lowering of the outturn SO incentive figure.

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