

ESB International Investments Ltd

**UK Office**

3<sup>rd</sup> Floor, Regent's Place, 338 Euston Road, London NW1 3BT, England  
**Telephone** +44-0-207-544 8631 **Fax** +44-0-207-544 8580  
[www.esbi.ie](http://www.esbi.ie)

Jenny Boothe  
Industry Codes and Licensing  
3<sup>rd</sup> Floor  
Ofgem  
9 Millbank  
London SW1P 3GE

9 October 2009

Dear Jenny,

**ESBI response to “Code Governance Review: Governance of charging methodologies: Initial proposals”**

ESBI welcomes the opportunity to respond to Ofgem’s consultation on its initial proposals for the governance of charging methodologies. As a developer of wind and larger-scale conventional generation, the governance and mechanics of network charging are critical considerations for our business.

*ESB International*

ESB International (ESBI) has been a developer of independent generation projects in the GB market for over fifteen years. We currently have interests in the 350MW Corby power station, in the 850MW development at Marchwood, which is due for commissioning later this year, and have recently announced our latest 860MW development at Carrington and 960MW Centrum development in Burton upon Trent, which are planned to commence operation in 2013 and 2016 respectively. We also currently have a number of live transmission connection applications and offers for Combined Cycle Gas Turbine (CCGT) developments at various locations across GB. It is ESBI’s intention to build 3GW of thermal generation in Great Britain in the next decade.

In addition to expanding our conventional generation portfolio, we are also seeking to expand our GB portfolio of renewable generation sites, having recently announced the acquisitions of Fullbrook Down and West Durham windfarms. All these developments are set within the context of a €22billion package announced by the ESB group to facilitate the transition to a low carbon economy.

**Summary of views**

We have provided more detailed views on the questions you raise in the consultation but prior to that have offered a more general summary of our views on some of the high-level points of principle raised by the consultation.

In general, we support the principle of increasing transparency and accountability in the governance of the various charging methodologies that are applied to the various energy networks. We also support increased industry participation in the development of the principles and mechanics that underpin those methodologies. As such, we welcome Ofgem’s review of



this area as part of the Code Governance Review but have a number of concerns on the proposals contained in the consultation.

Ofgem appear to favour options which would, in our view, result in unnecessarily fundamental changes to the existing charging governance structures. We are of the view that there are more proportionate options which should also be explored in terms of costs and benefits for both NWO's and industry participants. We present one such option below which would, in our view, provide significant benefits with significantly less regulatory burden than the options favoured by Ofgem.

We are concerned that the options favoured by Ofgem would significantly increase regulatory burden and note that this does not appear to have been adequately considered in Ofgem's consultation, particularly in its cost benefit analysis. Specifically, we are concerned that developing charging modifications under code modification processes would require significant additional resource to participate fully in the numerous working groups that would inevitably be required to develop increased numbers of charging modifications. One of Ofgem's aims for this review is to improve inclusion in the governance of charging methodologies. We were therefore surprised that Ofgem chose to only include large players that already participate in modification processes in its cost benefit analysis.

Volatility is a key concern for all parties who are subject to network charges. We note Ofgem has provided a number of possible mitigation measures which could be introduced to counter increased volatility resulting from multiple parties being able to raise charging modifications. Ofgem's proposal is that periodic windows be used to limit the flow of possible modifications. We are of the view that these measures would not reduce volatility; rather they would simply reduce the frequency of changes to charges. Under such arrangements, network charges would still be subject to material and highly unpredictable step changes as the periodic modification window took effect. We would therefore urge Ofgem to consider volatility not only in terms of timing but also in terms of charge differentials.

### ***ESBI's alternative approach***

We are concerned that Ofgem has limited its choice of options only to ones which involve relatively fundamental changes to the existing governance arrangements. We are of the view that the existing arrangements for electricity transmission could provide a sound base upon which to develop a more formal process. The electricity transmission charging regime provides opportunities for interested parties to raise issues and modification proposals at the Transmission Charging Methodology Forum (TCMF) and Charging Issues Standing Group (CISG). These groups have proved effective in providing interested parties with opportunities to discuss any concerns with the charging methodologies and possible modifications to them. Further, they have been shown to provide effective fora for parties to openly offer views, analysis and peer review. We note that similar arrangements are in place in the gas transportation charging arrangements.

We are of the view that Ofgem could provide a more proportionate solution to its view that the governance of the charging methodologies has inherent defects, by formalising the process currently used in electricity transmission. Parties would be able to formally raise issues which NWO's should then be required to give due consideration. This would include discussion at the relevant charging fora and where necessary the NWO should be obliged to provide support (including analysis) to proposed modifications. Where there is merit in a modification being taken forward, we envisage this being done under the existing governance structures. The key difference between this approach and Ofgem's "Option 2" is that modifications which are deemed to have little or no merit within the industry fora would not be required to be fully assessed and presented to the Authority for decision.

The changes described above would (in most cases) require only limited changes to licences but would result in greater transparency and industry participation in the development of the network charging methodologies. We are of the view that this would provide Ofgem with a more proportionate solution with the added benefits of it already being understood by industry parties and being able to be introduced with minimum change to existing arrangements.



## **Responses to specific questions**

### Chapter 3

Q1 Although we welcome Ofgem's attempt to provide qualitative analysis to support their options, we are sceptical as to the value of the results presented. In particular we are sceptical of the levels of capital expenditure (capex) that could be saved as a result of changing the charging governance arrangements. If the proposals brought forward by industry were only based on the better facilitation of the charging methodologies' objectives, we agree that there may be a reduction in capex. However, we are of the view that parties will bring forward charging modifications to better serve their commercial position (ie reduce their network charges) rather than to specifically better facilitate the relevant charging objectives. As such we think that, more than likely, the proposals would not result in the stated network capex savings. In summary, we believe that the degree to which capex could be saved is dependent on the charging mechanism and resulting charges and much less the governance arrangements that sit behind them.

Ofgem states that one of its aims in reviewing charging arrangements is "to improve inclusive, accessible and effective consultation". We note that Ofgem has assumed that no additional cost would be incurred by small players and that 10 large players would continue to dominate the assessment of each modification. By not including any increase in the costs incurred by smaller players' in considering and participating in the consultative processes for options 2, 3 and 4, we are concerned that Ofgem concedes that its proposals will not improve participation by smaller parties outside of the incumbent large players. We would therefore be concerned that these proposals will have an adverse impact on the development of effective competition in the markets to which the network charges apply.

Q2 We recognise that Ofgem had difficulty modelling the costs associated with charge volatility and agree that such costs are difficult to forecast given the number of unknown factors that contribute to them. However, it is our opinion that to not include any assumptions or analysis is remiss and should be addressed before any option is taken forward.

### Chapter 4

Q1 As we have discussed previously, we do not support any of the options presented by Ofgem in its consultation. We strongly of the view that our proposed alternative approach (described above) provides a more proportionate and less costly alternative to those provided by Ofgem and as such should be considered further. However, if we were to provide a view on the "least-worse" option, this would be Option 2.

Q2 We see no reason why there should be any prioritisation in changing the governance arrangements. Ofgem's primary reason for wishing to prioritise changes to the transmission governance arrangements appears to be the possibly significant increase in the levels of investment (and subsequent revenue to be recovered) that could be seen as a result of the revenue drivers it allowed the TO's at TPCR5. We are firmly of the opinion that the amount of revenue to be recovered should not (in itself) be a driver for change. Were individual parties able to raise modifications to mitigate the effect this increased investment may have on their absolute charges, we are of the view that many would attempt this to the significant detriment of charge stability and predictability. If Ofgem is of the view that the network charging methodologies have identifiable defects in their governance structures, then these should be addressed at the same time.

Q3 We do not agree that creating modification windows will mitigate increased charge volatility. A charge window would only address the timing element of volatility and would have no effect on mitigating significant changes in charges that would inevitably result from all of the proposed options.

Q4 Considering the decision timescales for larger, more complex (or contentious) modifications we are of the view that neither 3 nor 4 months would be sufficient. It is worth noting that were option 3 to be taken forward, the decision timeline could be especially long as Ofgem currently has no specified period in which it must make a decision under some code governance procedures. We would welcome further clarification from Ofgem on how it would



manage such modifications to avoid significant delay in them being determined and implemented (as has happened with CAP148).

Q5 The alternative approach we have proposed would not require any definition of an affected party as it would allow any interested party to attend the appropriate charging forum and formally require an NWO to look at aspects of the relevant methodology about which it feels there may be a defect. Alternatively, any interested could formally submit its own modification to the forum and NWO for wider consideration and possible development.

### ***In conclusion***

While we welcome Ofgem's intentions and review of this area of industry governance, we are of the view that there remains areas in which Ofgem should do further work on its proposed options for change. Network charging methodologies and the governance arrangements which underpin them are critical considerations for all industry participants. As a developer of generation we are acutely aware of the key role network charging plays in our investment and operational decisions. We would not want to see a situation whereby significant uncertainty and volatility is introduced into the charging regime with little discernable benefit. Were this to be the case, we are strongly of the view that vital investment in new, more efficient and less polluting generation would be affected. In a time when industry is striving to meet Government's targets for carbon reduction whilst ensuring security of supply, stability and clarity in network charging regimes is critical.

Should you wish to discuss any aspect of this response (in particular our alternative proposal) further, please do not hesitate to contact me.

Yours sincerely,

**Michael Dodd**  
GB Regulation Manager

By e-mail

