

Mr. Ian Marlee
Partner, Trading Arrangements
Ofgem
9 Millbank
London
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26 March 2010

RE: GAS SO INCENTIVE PROPOSALS FROM APRIL 2010

Dear Ian,

Centrica welcomes the opportunity to comment on the issues raised in the final proposals consultation on the System Operator Incentives for April 2010. This response is on behalf of the Centrica Group excluding Centrica Storage Ltd. There is no confidential information contained within this response, which covers the gas SO incentives proposals only.

Chapter 2:

Question 1: Do you consider that the final proposals for the SO incentive to apply to NGGs external SO costs represent a fair balance of risk and reward?

Centrica welcomes and agrees with a number of items contained in the final proposals, including changes to the demand forecasting incentive.

We also welcome the proposal to align SO incentives with price controls and to review the Environmental and Operating Margins incentives for 1 April 2011. We would also like to put detailed effort into analysis of a number of other important issues such as UAG, GCRP uplift and residual balancing at an early stage rather than leaving them until shortly before 1 April 2012. The rollover of TPCR4 may, however, mean that it would have been better to use one year schemes now and two year schemes from 1 April 2011 rather than having a number of one year schemes from 1 April 2012.

We are, however, surprised by the change in the Price Performance Measure, which was not signalled in the initial proposals from National Grid and where the final proposal may provide a perverse incentive for National Grid to concentrate too much on the linepack incentive if the PPM target is inside the default bandwidth. We considered that the parameters of the current scheme were appropriate given the current default gas cash-out price values and the continued existence of the linepack incentive. The application of incentives needs to be balanced such that one incentive should not act in the opposite direction to another incentive.

Overall Centrica agrees that there are a number of improvements to the gas incentive schemes included in the final proposals. We are not convinced, however, that the package of incentives proposed appears to be providing the right balance between risk and reward. In particular the introduction of longer-term incentives should be accompanied by either widening of caps and collars or else the use of continuing upside/downside, but at reduced rates of impact, as is currently in the case of demand forecasting, although this is only one-sided at the present time.

Question 2: Do you consider that the proposed licence modifications appropriately reflect the final proposals as described in this chapter?

In terms of the algebra the parameters in chapter 2 of the proposals document appear to have been successfully transferred into the proposed licence modifications.

There is one aspect which is not completely clear, however. With respect to the two new tasks, namely development of a Linepack product and updating the default values of system marginal prices, while there is a requirement for reporting on progress every 4 months there is no indication whether these reports will be published in any form.

Please do not hesitate to contact me should you require further information about any of these responses.

Regards,

Clive Woodland
Planning & Analysis Manager