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Update consultation on National Transmission System (NTS) flexibility capacity December 2010

Dear Lewis,

Thank you for the opportunity to comment on this consultation. This response is provided on behalf of the RWE group of companies, including RWE Npower plc and RWE Supply and Trading GmbH.

With the development of flexibility indicators following implementation of UNC0195AV¹ and the upcoming RIIO-T1 and RIIO-GD1 processes, it is timely to consider the system flexibility capacity arrangements. We agree with the principles and framework for the further development of system flexibility provision set out by Ofgem and in particular that the flexibility is a system-wide issue. However, we believe that assessment of system flexibility should be focussed upon flexibility required in operational timescales and, in our view, the consultation confuses flexibility and capability. In principle, we think that this flexibility is better managed, in aggregate, by the SO rather than allocated ex ante to individual Users. Any change in such an aggregated approach risks undermining competition and liquidity in the GB gas market.

The flexibility indicators presented to the industry to date show no discernable trends and although a number of key drivers and influences on future system flexibility requirements are forecast to change flows on the NTS, there is no conclusive evidence that flexibility is likely to be scarce.

Although there might be merit in including flexibility reporting requirements, together with specific output measures, in RIIO-T1, this would need to be enhanced by network analysis based on detailed modelling. However, we believe that there needs to be a significant burden of proof that there is a problem and that investment is the solution. There may be other, commercial or contracting solutions that would meet requirements. Our preference remains for any investment

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¹ Introduction of Enduring NTS Exit Capacity Arrangements

to be guided, at least in part, by user commitment. This is probably more relevant at the NTS/GDN interface where we think that GDN flexibility bookings could be part of the overall efficiency incentives on GDNs to meet their capacity obligations.

Our answers to the detailed consultation questions are set out in Appendix 1, below.

We hope these views are helpful and if you wish to discuss any aspect of them in further detail, please do not hesitate to contact me.

Yours sincerely,

By email so unsigned

Charles Ruffell
Economic Regulation

APPENDIX 1: Consultation Questions

CHAPTER 1: Flexibility capacity on the NTS

Question 1: Do you agree with our definition of system flexibility?

Ofgem's definition is too wide and confuses system flexibility with system capability. We believe that the definition of system flexibility should be limited to flexibility available within operational timescales, rather than investment timescales.

Question 2: Do you agree with our view that the ability to vary gas flows on entry and exit is valued by Gas Distribution Networks (GDNs), Transmission Connected Customers (TCCs), Aggregated System Entry Point (ASEP) operators and gas shippers?

Flow variations may arise for a variety of operational as well as commercial reasons. At an aggregate level, variations may offset each other, reducing the system management actions undertaken by the SO and overall costs to consumers.

CHAPTER 2: System flexibility drivers and indicators

Question 1: Do you agree with the system flexibility indicators developed by NGG?

The system flexibility indicators provide a useful framework to monitor and report on supply, demand and linepack variations.

Question 2: Do you consider that the system flexibility indicators are capable of identifying future system flexibility investment needs?

No. The current system flexibility indicators can only show historic patterns of flexibility utilisation and identify emerging trends in utilisation based upon those patterns. We do not think that they can be used as a reliable indicator of future investment needs on their own. Our understanding is that exit flexibility is assessed through network analysis based on a set of key modelling assumptions relating to the supply and demand for gas. In addition, they would need to be considered in the context of any wider regulatory developments that might drive different patterns in the future.

Question 3: Do you agree with our high-level analysis of the factors likely to affect future gas flows on the NTS? Are there important trends which we have not considered?

The high-level analysis includes all the major factors likely to affect gas flows on the NTS. Although these factors are forecast to change the patterns of NTS flows, at both entry and exit, the extent to which these result in the requirement for additional flexibility remains to be seen.

CHAPTER 3: Prevailing exit flexibility capacity arrangements

Question 1: Do you agree with Ofgem's representation of how shippers and TCCs manage their NTS exit flow variation requirements?

Yes. It is an accurate description. It should be noted that the UNC also contains provisions that allow NGG to reject OPN changes and to keep entry and exit renominations under review. These provide further incentives on shipper Users to meet their flow variation obligations.

Question 2: Do you have any views on the effectiveness of the existing UNC Offtake Capacity Statement (OCS) process applying to GDNs' NTS exit (flex) capacity bookings and do you consider that the UNC adequately supports shippers flexibility capacity needs?

We can only comment in general on the OCS process as we are not party to it and have little visibility over it following Ofgem's rejection of Modification Proposal 139A. The OCS process appears to be an effective mechanism for NTS to agree the GDNs' capacity requests, but is not particularly transparent. Although there are no strongly discernable patterns in GDN flexibility booking behaviour, the trend appears to be upwards, in part as result of GDN interruption reform. Given indications of possible locational constraints arising from increased GDN demand for flexibility, incentives on GDN flexibility bookings should be included in the overall efficiency incentives on GDNs to meet their capacity obligations.

From a shipper perspective, the current UNC supports shippers' needs.

Question 3: Would it be appropriate for NGG to consider investment to provide GDNs with incremental exit flexibility capacity?

This should only be considered where it is the most economic and efficient solution. The GDNs, as regulated monopolies, have a licence obligation to meet 1-in-20 peak day capacity demands on their networks. Their price control controls contain explicit incentives for them to meet these requirements efficiently. As part of the trade-off between NTS Exit capacity bookings (Flat and Flexibility), investing in their own networks and/or accessing interruptible capacity, the GDNs should be able to signal a value for flexibility. Essentially, they should balance the costs of alternative investment options against interruption to meet their capacity obligations.

CHAPTER 4: Next steps in the system flexibility debate

Question 1: Do you agree with our view of the principles and objectives which should apply to the further development of the system flexibility capacity arrangements on the NTS?

There is now more information available to understand better the requirements for flexibility. We agree that flexibility is a system-wide issue and not limited to exit. We do, however, think there is a significant amount of further work required to justify any changes to the existing flexibility capacity arrangements and to define what any new flexibility product or service should look like. In this regard we continue to have concerns over the appropriate definition and design of a flexibility product or service which may lose the current diversity benefits of managing flexibility in aggregate across the system. Our view is that it is most efficient for the SO to manage flexibility at an aggregate system level, rather than allocating flexibility ex ante to individual users.

Managing flexibility at an aggregate system level is, in our opinion, a contributing factor why the GB gas market has developed to be the most competitive and liquid market in Europe. Allocating flexibility ex ante to individual users risks undermining this and should be avoided.

Question 2: Do you agree that it would be appropriate to introduce an obligation on NGG to report on system flexibility indicators under the RIIO-T1 framework?

There is merit in NGG continuing to report the system flexibility indicators, but if the requirement is simply “reporting”, we are indifferent as to whether this is under the current arrangements or through an obligation under the RIIO-T1 framework.

Question 3: Do you agree that it would be appropriate for NGG to justify any system flexibility investment proposals under RIIO-T1 with reference to flexibility capacity system indicators and specific RIIO-T1 output measures?

We agree that any investment proposals should be well justified and a strong needs case established. Flexibility capacity system indicators are unlikely to provide this and, in order to protect consumers from inappropriate risks and costs, any investment has to be guided, at least in part, by user commitment. However, we are not convinced that investment is required at this stage. Our understanding is that historically NGG has not invested to provide system flexibility and it exists as a by-product of the physical properties of the NTS. Consequently, it may not be possible to define meaningful output measures.

Question 4: Do you agree that the commercial and use of system charging arrangements should reflect any costs imposed on the system by NTS users' needs to vary entry and exit flows?

To the extent there are specific incremental investment costs, these should ideally be targeted rather than socialised. However, targeting costs is not straightforward at entry and where flow variations offset each other it is debatable whether there would be any costs to target.