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Dear Vanja

Impact Assessment on National Grid proposal CMP 192: enduring user commitment

The Renewable Energy Association gives below its response to the issues raised in your assessment of the CAP 192 proposal and its alternative options. As you know our members work on all types of renewable power and heat projects including many electricity generation projects that are dependent on the transmission system. The imposition of a significant liability for transmission reinforcement costs and in particular the requirement for guarantees in respect of those costs has proposed a disproportionate burden on in particular small companies and small projects that has led to many otherwise sound projects not being taken through to completion.

Our headline points

The main points that we would like to get across are:

Minimising overall costs to the consumer

Ofgem's principle duties include protecting the end consumer, which includes factors relating to security and economy. Investment in the electricity industry over the next decade is going to be large. The largest part of this will be investment in new generation which will exceed investment in transmission by a factor of between five and ten. It is therefore far more important when protecting the consumer to maximise the efficiency of investment in generation than in transmission. Whilst superficially it is a generator's investors who lose money if a generation project goes wrong or becomes stranded, in the end customers pay as this puts up the cost of capital for generation investment.

In other words it is better for the end customer if a few percent of transmission investments turn out to be unnecessary than that this is reduced at a cost of far more by decreasing the efficiency of investment in generation by a few percent. Increasing the level of post commissioning commitment and imposing large liabilities on generators / requiring large guarantees, particularly at an early stage of project development, has the potential to lower the efficiency of the generation investment and closure process to the detriment of the end customer, even if there is some smaller reduction in abortive transmission investment.

Proportionality of guaranteed amount

In our view and in light of the above the main purpose of requiring a guarantee from generators is to avoid frivolous connection requests from causing Transmission Owners to invest in extra capacity that has very little chance of being utilised. One cannot have perfect foresight and inevitably there will be some investment whether it is in transmission, generation or distribution that with perfect foresight will have turned out to have been unnecessary. It is important to minimise this but this is not achieved by concentrating on minimising a relatively small component of it (transmission investment) if the result of that is a bigger inefficiency in generation investment and which forms a more significant proportion of customers bills.

Something along the lines of the German KraftNAV (Grid Connection Ordinance) of 2007 whereby to reserve transmission capacity generators have to pay €1000 per MW which is credited or refunded on connection, would be quite sufficient to discourage non serious connection requests.

A relatively large number of relatively small projects has a lower risk than a small number of larger projects

Many of our members' projects are relatively small but in combination with others precipitate significant transmission investments. A lot of these investments in strategic wider works are in reality at very little risk from the failure of one or two of these projects as either they would still be required for the remainder of the projects in an area or other projects in the area are very likely to come forward to replace the ones that terminate.

Response to the specific question asked

CHAPTER: Four

Question 1: We welcome stakeholders' views on whether we have identified all the relevant impacts of CMP 192.

You do not appear to have considered the effect of longer notice periods on post commissioning plant leading to the possibility of a lower level of generation

adequacy and / or higher electricity prices for end consumers due to a reduction in the level of flexibility in generators timing their closing decisions more than cancelling out the increased efficiency of transmission investment planning.

Question 2: Do stakeholders agree with our assessment of the potential environmental impacts of the proposal?

We do not think that the proposals will make any difference to the status quo as regards the environment.

Question 3: We seek stakeholders' views on the potential implications of the potential perverse incentives, and views as to how they may be mitigated.

We agree with the premise that one should not ask for security to cover assets that are already built so given that it may often be the case to be sensible to oversize assets there is little that can be done about users deferring their connection until after assets have already been built. One would presume that the signals in the market / capacity mechanism / low carbon incentive mechanisms should be correctly set so that deliberately holding back like this should only be profitable if earlier delivery of the project would have been of limited value.

What is more worrying in terms of perverse incentives is the incentive for existing plant to announce closure four years ahead and feel compelled to live with that decision irrespective of what may be required nearer to the event.

CHAPTER: Five

Question 4: Do stakeholders agree with our summary of the impact of the CMP 192 original proposal on pre-commissioning generation?

We have not found any obvious errors in your summary.

Question 5: Do stakeholders agree with our current thinking that placing a four-year liability for wider works on pre-commissioning generators is appropriate?

No. We think that a reduction in the period of liability for wider works for pre commissioning users would be appropriate as it is very unlikely (more so than for local works) that the wider works investment would be stranded even if the generator terminated its agreement.

Question 6: Do stakeholders agree with our view that the proposal to halve the liability on generators for local works that are designed to accommodate demand, either existing or in the future is not appropriate for the reasons set out in this chapter?

No. The liability reduction of 50% for wider works for generators on the basis that demand benefits applies in the same manner to local works where those works will supply demand. We cannot see any argument for a 50% reduction in one that does not apply to the other as well.

Question 7: Do stakeholders agree with our view that the proposed credit cover arrangements are appropriate and provide valuable protection to consumers?

It is felt by many small and medium sized generators that the requirement to post security gives an unfair disadvantage to them compared to the larger players and is thus a barrier to competition.

CHAPTER: Six

Questions 8: We seek stakeholders' views on the extent to which asset health and the associated plant life assessment could hinder generators in providing four-year user commitment notice.

Clearly users can give a four year (or any other period) notice of closure period if that is what the rules say they have to do. The issue is whether increasing the notice period does not increase costs by more than any consequent saving in transmission investment costs might reduce them. Parties will be reluctant to take a risk of not giving notice when they are at an age to risk an uneconomic to repair plant fault occurring so are likely to give notice of closure for an earlier date than they might otherwise have done had they been able to give the notice at a later date. This risks a reduction in security of supply and / or an increased cost to customers due to generation plant closing on average earlier than it would otherwise have done had it been able to give a shorter period ahead closure notice.

Question 9: We would be interested to hear stakeholders' views on whether we have appropriately identified all the relevant interactions with other policy developments, and potential impacts on user commitment arrangements in general and more specifically, our consideration of CMP 192 proposal.

In addition to policy developments it is important to consider the uncertainties in market fundamentals that make it much more difficult to predict whether it is appropriate to give closure notice at the four year ahead stage. For example it is much more difficult to be accurate in assessing new plant delays at the four year ahead stage than over a much shorter period ahead and with the amount of new plant build potential delays to its commissioning will be an important factor in the precise year when it would be sensible (from both an economic and a security of supply point of view) to close an existing plant.

Questions 10: Do stakeholders consider that a level of uncertainty associated with policies currently being developed in greater detail could hinder generators in providing four-year user commitment notice? Impact Assessment on National Grid proposal CMP192: enduring user commitment 54

Yes, not least because the uncertainty will also have an effect of the readiness of investors to come forward with new generation.

CHAPTER: Seven

Question 11: We welcome stakeholders' views on the analysis presented in this section and, where available, any additional information and/or analysis in relation to the impact of CMP 192 on the efficiency of network investment.

It is not clear from the text how the analysis has been undertaken. The value at risk is not the most important element – it is the "expected abortive expenditure" associated with different post commissioning notice periods. The fact that investment is at risk of being abortive does not tell one much without knowing what the probability is of that investment actually turning out to have been abortive. Even when one has that it would have to be balanced against the probability of security of supply being reduced and / or there being more investment in generation than would be necessary if shorter generation closure deadlines were in force.

Question 12: We seek stakeholders' views on the approach to risk adopted in National Grid's analysis and on the potential alternatives to assessing the risk.

The key point to reiterate is that there has been no analysis of the additional generation / security of supply costs caused by having a longer notice period for generation closures.

Question 13: Taking into account various factors discussed in this document that may have an impact on generators' ability to provide four-year notice and National Grid's analysis presented in this chapter, we seek stakeholders' views on the most appropriate length of the notice period for post-commissioning generators.

Our view remains that overall the consumer receives the best value for money when the generation notice period is as short as possible.

We hope that you find these comments useful. Please let me know if you would like to discuss them further.

Yours sincerely

Gaynor Hartnell

Chief Executive, Renewable Energy Association