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PROJECT TRANSMIT - WELSH GOVERNMENT OPINION

1. Further to our letter on Project Transmit to Alistair Buchannan of 6th December 2010, the publication of the Project Transmit consultation and associated Redpoint study papers on 20th December 2011 and the Welsh Government meetings with you in Cardiff and the Welsh Government presentation at the Project Transmit stakeholder event on 6th February 2012, we would confirm that the Welsh Government position on the Project Transmit recommendations are as set out below.
2. The Welsh Government fully supports the dismissal by OFGEM of the expensive socialisation option.
3. The Welsh Government notes the OFGEM comment in the consultation paper that the choice between the improved ICRP Option and retaining the status quo is not clear cut but disagrees with the OFGEM initial view that the improved ICRP is the right direction for transmission charges. From a strong sustainable development viewpoint, we believe that it is the wrong direction for the following reasons:
 - Our experience in discussions with NGET and others on the grid requirements of major wind farm projects indicate that in the improved ICRP model, the differentiation of circuits between “peak security” and “year average” looks artificial in the real engineering world.
 - This view is strengthened by our participation in the discussions in the Electricity Network Steering Group and elsewhere which have always indicated that transmission operators will be trying, if at all possible, to ensure that the peak output from large wind farms is not constrained by the system and thus will reinforce the grid infrastructure accordingly. This would appear to be confirmed by the fact that the £5billion plus of transmission operator investment that OFGEM is currently backing to reinforce the Scottish grid and the Scotland-England inter-connectors is clearly designed to cope with the peak output of wind farms in Scotland, not simply 70% of that output which would appear to be the basis of the improved ICRP calculation.

- Further, we also note that the Project Transmit technical working group paper itself accepts that for wind farm developments, there is not a linear relationship between transmission grid reinforcement costs and load factor.
4. As well as these technical considerations, we have significant economic and systems concerns. As the Redpoint analysis has partially done, we believe one must look at the economic and total system consequences arising from your proposals. Socialisation is rightly dismissed as being very expensive and we would draw your attention to the extent of existing fuel poverty in Wales which is featured in figure 14 of your consultation document. We have a number of concerns with regards to the consequences of moving to an improved ICRP:
- The improved ICRP model clearly incentivises intermittent generation over base load station. This was raised by various parties at the 6th February stakeholder meeting and is recognised in the Project Transmit technical working group report but dismissed there as not relevant to pure transmission issues. We cannot agree with that position: from the Nation's and consumer perspectives, one must be concerned about the total system cost and security of supply issues, and not focus on any artificial distinction between generation, distribution, transmission or supply.
 - The Cost Benefit Analysis results for the improved ICRP in the Red Point report suggest that the one benefit for power sector costs over the status quo is a fall in generation costs. In other words, the only benefit is a rise in profits for generators. Transmission costs, constraint costs and carbon costs are all due to rise compared to the status quo. The rise in these costs seems counterintuitive to the sustainability agenda of this project.
 - Renewable energy generation forecasts are similar for both the improved ICRP and status quo. However, given that under improved ICRP it would appear to change the profitability of generating plant according to their location it stands to reason that some areas of the United Kingdom would benefit to the detriment of others. The evidence suggests that Scotland would benefit considerably despite the fact that the majority of the electricity demand lies in the south of the UK. A producer surplus would undoubtedly result with UK consumers having to pick up the cost of moving surplus energy should new transmission infrastructure be required. We do not think that this is a rational use of the transmission network given that by definition existing infrastructure will be underutilised.
 - One of the drives for change should be to ensure that the UK meets its EU renewables target in the most cost effective manner and in a way that delivers value for money for consumers. A concern with the proposed improved ICRP is that it interferes with market signals which would help achieve this. The status quo system internalises costs with transmission investments and costs being a function of the distance over which power is transported. The Redpoint report argues that the current system of very high charges in some remote areas could present a barrier to exploiting the best renewable sources and jeopardise hitting the decarbonisation targets. We would suggest that it is the job of government through its RO and soon to be CfD market to provide the incentives for renewable generation and that the TNUOs should continue to internalise costs as with the status quo.
 - Some concern that a move to an improved ICRP would penalise baseload low Co2e generation. This could have an impact on nuclear and biomass plants in Wales. A move under the proposed new ICRP to a peak and year round tariff that effectively benefits remote renewable generation could have a detrimental effect in encouraging the development of CCS on peak generation. As highlighted above, the concern is that an improved ICRP interferes with market signals and could distort the market from delivering the UK renewables target in the most cost effective way.
 - The estimates of lower generation costs to certain generators in specific locations under the improved ICRP has not been sufficiently linked back to consumer impacts. Indeed the Red

Point analysis implies a £900 million cost to consumers over and above the Status quo. We feel more analysis is needed to explore this link.

- The Red Point analysis estimates a move to the improved ICRP could add £1.50 on the average consumer bill. We feel that the analysis concerning the impact on consumers has generally been underdeveloped. For instance we would prefer to see specific analysis on the link with Fuel Poverty. In addition, with major changes in the UK energy market being driven by the EMR we have a concern about analysing the impact on consumer bills from an improved ICRP in silo. A more robust analysis of the impacts on the consumer sector would involve some cumulative analysis so that any changes in bills from other policies in the pipeline were looked at as a package.
 - There is a clear disincentive with improved ICRP to install large battery grid storage at the wind farm level, something almost all experts would recognise as highly desirable.
 - The improved ICRP proposals advantages low carbon generation in areas remote from demand such as Scotland and disadvantages projects in areas close to demand such as the south of England and Wales – whether these projects involve low-carbon electricity from intermittent wind, flexible biomass, periodic tidal or nuclear. This is not economically sensible from a cost effectiveness perspective. The Red Point report specifically suggests that there could be a geographical shift in favour of wind farms in Scotland and that wave and tidal projects would face more favourable tariffs in Scotland and less favourable tariffs in England and Wales versus the status quo. In this context, it is also important for OFGEM to take account of the different RO regimes in England and Wales, Scotland and Northern Ireland respectively. The ability of the devolved administrations in Scotland and Northern Ireland to set their own RO banding levels already disadvantages Wales and the proposed changes set out in the improved ICRP compounds the unfavourable investment conditions for some technologies in Wales.
 - The use of load factor considerations in the improved ICRP does not differentiate between intermittent output from wind and the periodic output from tidal, whether from barrages or tidal stream projects. The system balancing requirements between wind and tidal are very different and in practice very much less expensive for the latter.
5. We therefore believe on balance, particularly taking in the wider issues which the OFGEM consultation document itself recognises as important, leads to the preferred option being the retention of the status quo.
6. Finally, as at the Project Transmit stakeholder event in February, might we flag that any change in the split of transmission charges between generators and consumers in favour of generators requires very careful consideration. Both the Project Transmit technical working group report and the Redpoint analysis assumes that this change is effected simply because it might be required in the future by EU internal electricity market considerations. This may or may not be the case, especially if the internal market discussions on Europe begin to focus as they should on carbon content issues. Since a switch of costs from generators to consumers is likely in practice to increase the final costs to the consumers, we would flag the importance of a proper impact analysis being undertaken to illuminate the situation.
7. We are happy to discuss these points in more detail with yourselves or other experts however, we can not endorse the move to improved ICRP

Yours sincerely

Dr R. Loveland

Energy Adviser to the Welsh Government

