

Flexibility and Capacity Working Group

Minutes of the 6 th meeting of the Flexibility and Capacity Working Group	From Date and time of Meeting Location	Ofgem 11 July 2012, 10:00 – 14:00 Ofgem, 9 Millbank	16 July 2012
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1. Present

Name	Organisation
Dora Guzeleva	Ofgem
Anna Rossington	Ofgem
Mark Askew	Ofgem
James Hope	Ofgem
Thomas Johns	Ofgem
Nicola Meheren	Ofgem
Donald Smith	Ofgem
James Goldsack	Ofgem
John Christie	DECC
Graeme Vincent	SP
John Gray	SP
Fruzsina Kemenes	RWE Npower
Zoltan Zavody	RenewableUK
David Walker	West Coast Energy
Nigel Turvey	WPD
Keith Hutton	UKPN
Duncan Carter	Consumer Focus
Keith Noble-Nesbit	NPG
Iain Miller	NPG
Mark Drye	NPG
John France	NPG
Paul Bircham	ENWL
Steve Cox	ENWL
Gareth Shields	SSE
Stewart Reid	SSE

2. Updates

2.1. Minutes from the FCWG meeting on 20/06 were considered. JC raised a concern over the implication in the minutes that the scenarios put forward by DECC are temporary and proposed changes to paragraph 5.1 to highlight that the scenarios are based on the 4th Carbon Budget. The proposed wording was agreed and the minutes were approved.

2.2. DG and JH went through the update table for other work streams. ZZ highlighted that WS6 could look at customer relationship with DNOs and the group was advised that there is an action on a member of WS6 to that effect. In response to questions concerning the WS6 first report draft outline, FCWG members were invited to submit comments to DG.

Action	Person - By
Send any comments on SGF WS6 report outline to DG who will forward them to WS6.	All – 23/07/12

- 2.3. DG updated the group on the recently published SGF WS3 report and next steps to find out how DNOs will break down the model in the different licence areas.
- 2.4. JH explained ongoing work of the Reliability and Safety Working Group investigating ENWL's proposal on LIs. The group was also made aware of an online consultation on guaranteed standards.
- 2.5. The group was updated by DG on concerns raised in the Connections Working Group concerning implications of a "time to connect" incentive on competition.

3. DG incentive

- 3.1. AR talked through Ofgem's slides on the DG incentive and asked for views on the pros and cons of the incentive.
- 3.2. The financial benefit seen by the DNO due to the DG incentive was discussed and AR stated that in the DPCR4 period, benefits were very small. PB highlighted that the 80% pass through mentioned in the slides is highly conditional on the DNO meeting certain criteria, therefore further limiting the benefits to the DNO.
- 3.3. It was agreed that the implication of the DG incentive on the transmission system is an issue as developers can be hit by costs charged by the TSO and passed on by the DNO when connecting a DG development.
- 3.4. There was a consensus for National Grid to be invited to talk at the next FCWG meeting on 1 August. However, FK highlighted that this may be a topic best discussed in the Connections Working Group and DG agreed to discuss this with the group's chair.

Action	Person - By
Discuss with chair of connections working group to decide where issue of DG connections that incur National Grid fees should be dealt with and invite NG to next meeting to discuss rationalisation of NG process/fees regarding DG connections.	Ofgem – 20/07/12

- 3.5. There was a discussion of the problem of how to apply the DG incentive in practice with IM arguing that it is sometimes better for the DNO to ignore the DG incentive and treat connections of DG as standard connections.
- 3.6. SC ran through ENWL's slides on the DG incentive, examining three areas: what drives cost, what issues are important for RIIO ED1 period, and where does the DG incentive work to incentivise the increase in capacity for DG connections?
- 3.7. SC explained the cost drivers for networks with constraints at different voltage levels and argued that the predominant problems for DNOs are the system fault level and voltage rises rather than load increase.
- 3.8. DW argued that the options of undergrounding/overhead and the routing of cables should be included in the table of cost drivers and these were largely supported as issues to consider.
- 3.9. It was noted that transparency of information provision relating to DG connections is an important area and can be improved.
- 3.10. There was a discussion of whether the DNOs should provide prospective DG developers with information on the cheapest locations to connect to the network. SC and others raised concerns over the number of speculative connection applications they receive in order for developers to find the cheapest connection location. The suggestion that DNOs create a map of good connection locations for DG was met with some

agreement from the group. Those who agreed saw a benefit from reduced numbers of applications though there was concern that it may not be a straightforward exercise.

- 1.1. DW argued that developers never know whether the DG incentive is being applied in each case. It was noted that the DNO and developer should engage in dialogue over connection requirements but SC highlighted that this is not practical given the quantity of applications received and the short timescales involved. DG argued that GSOP allows the customer to stop the clock in order to have this dialogue.
- 3.11. SC suggested that the DG incentive creates a “catch-22” situation, arguing that if the DNO invests but DG demand does not arise, 100% of the risk is borne by shareholders and is deemed inefficient by Ofgem ex post. However, if there is evidence that developers want to build DG in an area, the DG incentive is no longer applicable.
- 3.12. SC asked what the purpose of the cap on the incentive rate was and argued that it meant DNOs are not incentivised to invest in smart solutions for cost-saving purposes. DG responded that the cap was put in place due to the rough forecasts of demand.

Action	Person - By
Comment on ENWL slides. See if cost drivers table is relevant to their network and if any conclusions are different. Also consider overhead/undergrounding and routing as cost drivers.	DNOs – 26/07/12

- 3.13. DG laid out seven questions that need to be answered by the DNOs:
 - 1) For new/modified connections above LV, do any mechanisms (apart from the DG incentive) incentivise low connection costs for DG? Is there a market failure that requires a mechanism such as the DG incentive to tackle it?
 - 2) Are there any types of LCT at HV not covered by DG incentive?
 - 3) Are there benefits that DG can introduce to the network and if so, are the benefits of DG recognised sufficiently in the current charging and incentive mechanisms?
 - 4) Do we need to specifically focus on sole use assets?
 - 5) How would removing claw-backs change the incentive on undertaking anticipatory investment?
 - 6) Are forecasts accurate enough to no longer need a cap on the DG incentive?
 - 7) Should DNOs take responsibility for highlighting to developers where it is likely to be cheap to connect DG?

Action	Person - By
Provide comments/answers to the 7 questions above.	DNOs – 26/07/12

- 3.14. The group discussed question 1. IM argued that DNOs have a statutory duty to reduce cost and MD added that connection competition drives costs down. However, SC argued that as investment covered by the DG incentive does not go into the RAV, it is therefore not covered by the IQI and therefore is lacking this extra incentive.
- 3.15. PB argued that the DG incentive introduced a market failure and that IQI would work for DG connections, suggesting a separate RAV for DG to prevent socialising costs.

- 3.16. ZZ noted that it is important to think about when an incentive around DG will no longer be required.
- 3.17. Addressing question 2, SR argued that the incentive should be as open as possible in order to stimulate innovation and cover uncertainties around LCT and DG penetration volumes in the RIIO ED1 period.
- 3.18. The group discussed question 3. DG argued that before connection, price signals should be sent that allow proponents of DG to share in the network benefits it produces. SR said that the IQI already does this and no separate mechanism is required.

5. Discussion of outputs and incentives

- 5.1. MA ran through Ofgem's slides and explained the responses to questions on outputs.
- 5.2. The group discussed the proposition in option 1: that no additional output beyond CIs and CMLs are required. PB argued that the IIS will incentivise efficient delivery of low CIs and CMLs but may not provide full-life efficiency for network assets. There was a general consensus with this view.
- 5.3. IM raised a concern over the wording in the slides suggesting that focussing on CIs and CMLs could lead to over-investment. IM highlighted that in Northern Powergrid's response, it was argued that this could happen only in marginal cases and that this is balanced by IQI. MA agreed to adapt the slides before publication to take note of this discrepancy.
- 5.4. DC proposed an asymmetrical negative incentive but JH warned against such a move, explaining that this approach had failed to produce sustained performance increases in the past.
- 5.5. The group discussed option 2: that LIs are used as an additional output measure alongside CIs and CMLs. MA explained that the concern is that without LIs, DNOs are liable to inefficiently sweat their assets. SR responded that DNOs are squeezed between IQI, CIs and CMLs to only sweat assets up to an efficient level.
- 5.6. AR asked the DNOs whether they look beyond the price control when considering investment for reducing CIs and CMLs. All DNOs responded that they do. MD said that they assume incentives are neutral beyond the end of the price control, and PB said they make a probabilistic judgement of IIS remaining in the next price control.
- 5.7. Instead of using LIs, SR and JH suggested that the BMCS and GSOP tackle some issues around sweating of assets. SR highlighted that the fault cost allowance strongly incentivises avoiding faults as it is a finite pot shared through IQI.
- 5.8. The group discussed using LIs for forecasting and modelling purposes. SR argued that monitoring could provide more data with which to model successfully and PB argued that although the CI and CML predictions do not provide a strong enough incentive for strategic investment, the IIS does make DNOs respond quickly at time of need.
- 5.9. MA highlighted that in the slides the question should relate to "modelling" LIs on LV rather than "measuring" LIs. SR noted that LIs on LV will be of spurious accuracy and therefore could be misleading.
- 5.10. MA discussed the use of LIs as a secondary deliverable. PB agreed with this proposal and argued that if DNOs used comparable modelled LIs that measure risk, they could be a secondary deliverable which shows where assets are no longer efficient and therefore forces intervention – smart, commercial or conventional. DNOs could then

demonstrate how they have reduced the risk on their network over the price control period.

5.11. Conversely, SR argued that they often have to reinforce or invest due to voltage or power quality issues and therefore LIs would not be useful as a secondary deliverable.

5.12. DG asked whether there is a need for Ofgem to look back over a price control period to make sure DNOs have invested the money given to them. SR argued that this is not necessary as IQI and IIS push DNOs in the right direction. However, SC asked whether this means that if forecast demand never arises, should DNOs be allowed to keep the money.

5.13. DG asked whether IQI is applicable to new connections. IM talked through his note on this issue, highlighting that for EHV connections there is no correction mechanism on volume like there is at LV and HV.

5.14. The group discussed whether there are any additional outputs that are required. The consensus was that there is no need for LIs to be used to increase reliability as IIS and BMCS should deal with this but there remained a question mark over their use in uncertainty mechanisms.

6. A.O.B

6.1. Suggestions of possible locations for the next meeting on 1 August were asked for from the group. DG put forward three options: London, Birmingham and Glasgow. It was agreed that the meeting should be held outside London.

6.2. KH highlighted that some stakeholders who wish to attend were not present at the meeting and therefore should be consulted.

6.3. An indicative vote of those present showed an even split between support for Birmingham and Glasgow as potential locations. It was agreed that additional stakeholders should be consulted and then a decision made based on the majority decision.

Action	Person - By
Finalise location for FCWG meeting on 01/08.	Ofgem – 20/07/12

6.4. Proposed agenda items for the next meeting were agreed with the addition of a discussion of uses of LIs as a capacity measure.

6.5. DNOs were reminded to provide ZZ with comments on the paper on the role of the DNO.

Action	Person - By
Provide comments to ZZ for paper on role of the DNO.	DNOs – 18/07/12