ANNEX

CHAPTER: One

1. Do you agree with our proposal to put a balancing services incentive scheme in place for 2013-15?

For the purposes of a two-year scheme, we believe the proposal to continue with the balancing services incentive scheme, subject to greater assurances around NGET's modelling and how changes / updates will be made, is a practical way forward at this stage.

2. How much confidence do you have in the ability of the models to set a robust target given recent developments to the models and methodology?

Without sight of the models, we only have Ofgem's account of the models to go on. However, we believe the proposed mechanisms, namely the mid-period review, provide some comfort that Ofgem has put in place the mechanisms to correct and improve the models, within certain parameters, during the course of the scheme.

Notwithstanding the above, we believe it is essential that NGET's models are made public as part of the scheme, with sufficient input from NGET to give industry a chance to understand the models and to test them. If this is not considered feasible, at the very least, we believe an independent third party should be commissioned to audit the models and to report back to Ofgem or an industry group in advance of the scheme commencing. A precedent for this already exists in the Irish market whereby the 'Plexos' model, which is used to calculate the single electricity market system marginal price, is subject to third party validation.

CHAPTER: Two

1. What are your views on making balancing mechanism 'pseudo' prices an ex post input in the energy models? What additional considerations may exist?

Prior to making this change, it would be interesting to understand how different NGET's forecasting of its volume weighted average BM prices have been historically from actual outturn prices. This would give us a clearer understanding of the value involved in making this change. Moreover, we believe it is unrealistic to remove all elements of risk from the incentive mechanism. Indeed it could be argued that an incentive should only apply where there is some degree of risk, otherwise it could be questioned why it is required.

2. What are views on the appropriate length of time for input of transmission limits? What value do you place on having forecasts ahead of time which are as accurate as possible?

We place considerable value on NGET's forecasts and, recognising that NGET is best placed within the industry to provide these forecasts, the industry as a whole has provided NGET with considerable funding over the years to ensure that NGET has the means to make sure its forecasting is as good as possible.

Notwithstanding this, what is possibly of greater importance to us, particularly as a transmission owner, is that any changes to transmission limits are properly and effectively communicated and that care is taken to ensure that any changes do not dilute the Network Access Policies.

Going forward, we are conscious of the forthcoming requirements under the European Operational, Planning and Scheduling Code, which seek enhancements to the provision of outage information to the TSO by users. This could impact on the need for an incentive in this area.

3. What are your views on the requirement for, and appropriate level of, a discount factor to be applied to the constraints model?

We support Ofgem's position to retain the existing discount factor of 41%. Whilst we support ongoing assessment to establish whether this remains the 'right' discount factor, we would be reluctant to see a change to the forthcoming scheme at this stage, which may not have the opportunity to be robustly tested. Instead, we believe this ongoing work should be used to inform the subsequent scheme from April 2015.

CHAPTER: Three

1. Do you agree with our proposals for the key parameters of a BSIS?

We welcome the proposal to apply a two-year scheme; we concur that more confidence is needed ahead of applying an eight-year scheme, but agree that this should be the longer-term ambition.

We also support the proposal to run the scheme as two single years to ensure that the strength of the scheme in the second year is not adversely affected by NGET's performance in year one. Given concerns historically relating to NGET's models, we believe it is prudent to introduce a mid-period review. However, as set out, this must be subject to clear, well-defined parameters and any changes must be capable of being understood by the market and subject to market-approval.

2. What are your views on the one year update provisions and the requirement for income adjusting event provisions?

Please refer to our response to Q2 of Chapter 2 and Q1 of Chapter 3.

In terms of the ongoing requirement for income adjusting event provisions, we agree with Ofgem that the need for these provisions is eroded by the introduction of a mid-period review and indeed the proposed structure of two single year schemes.

3. Do you have any views on the types of inputs that may be suitable for adjustment as part of the mid-scheme provisions?

We believe the inputs eligible for mid-scheme adjustment should be kept to a minimum and clearly identified at the outset. These should be tightly limited to inputs that are vulnerable to external factors that NGET could not have reasonably been expected to account for ahead of the scheme commencing.

4. What do you consider to be the merits / disadvantages of applying the scheme retrospectively to the 1 April 2013? Do you consider this to be the best option for the 'interim period'?

The clear merit in applying the scheme retrospectively is that the incentive on NGET to behave in accordance with the scheme drivers is maintained without any breaks.

However, as we understand it, this is contingent on NGET agreeing in principle to the scheme without the necessary licence conditions. It is not clear, in practice, how robust this will be and indeed whether this will be realised. Presumably NGET will only agree to this if the scheme is favourable?

In terms of retrospective changes to BSUoS charges, this is clearly not ideal. However, if this is required, we agree that this is best made by adjusting future charges (rather than retrospective adjustments). Depending on scale, it may not be appropriate to apply as a single adjustment. We are mindful of the cap that Ofgem has put on the potential exposure. As we understand it, this is a 'best case' exposure. We would question whether the direction to modify NGET's licence is sufficient to trigger this recalculation of BSUoS charges or whether it would in actual fact not take place until September, some three months later.

CHAPTER: Four

1. What are your views on the additional incentives that we are proposing to include alongside a BSIS?

Discretionary reward: We agree with the latest proposals surrounding a discretionary reward element and the proposal to move to a reputational incentive on transmission losses given the parallels with RIIO-T1.

Wind generation forecasting incentive: As set out in our response to Q2 of Chapter 2, we place considerable value on NGET's forecasts, including its wind forecasts. We are therefore keen that NGET continues to drive improvements in this area and, as such, we support the proposed wind generation forecasting incentive. However, in order to ensure that the total error is used (as opposed to the 'net' error), we believe the incentive must rely on root mean square error.

Black start incentive: We do not believe NGET's proposals surrounding black start are sufficient to deliver the black start capability expected to be required going forward. We believe there is a more fundamental issue in terms of bringing forward black start capable plant: a disconnect in the understanding of the real costs to generators of providing this service. We believe this should be addressed ahead of any incentive on NGET's forecasting requirements.

2. In particular, what are your views on the merits of including a discretionary reward scheme alongside a BSIS? And what are your views on our proposals for the parameters of a scheme?

Our understanding of the discretionary reward scheme is that it encourages NGET to think beyond the two year BSIS scheme by funding the roll out and trial of more proven innovations. This is to be encouraged given the longer-term ambition to put in place a more enduring scheme beyond 2015.

In terms of the scheme's parameters, we believe it is right to scale this back to reflect alternative (but similar) sources of funding that are available through the RIIO framework. We have a slight concern that Ofgem has not fully addressed the potential for possible overlap between the different incentives, namely the Innovation Rollout Mechanism and Environmental Discretionary Reward under RIIO-T1. There is a lack of transparency between NGET's TO and SO functions and, as such, we believe there is the potential for the SO to benefit twice through both the RIIO-T1 and SO incentive frameworks.

3. What are your views on the additional incentives that we are proposing not to include alongside a BSIS?

4. Do you agree with our proposal not to include a BSUoS forecasting incentive? What measures could help to reduce volatility of BSUoS charging going forwards?

We had felt that there was benefit in incentivising NGET to improve its BSUoS forecasts. However, we understand the changes that have already been implemented (namely modification CMP 208), which should drive improvements in this area once it the modification has had time to properly bed in.