



Bringing Energy
Together

Consultation response:

Proposed Income Adjusting Event submitted by NGET Electricity Transmission plc in relation to the 2015-17 Electricity System Operator Incentives Scheme

14 July 2016

Context

The Association for Decentralised Energy welcomes an opportunity to respond to this consultation on *Proposed Income Adjusting Event submitted by NGET Electricity Transmission plc in relation to the 2015-17 Electricity System Operator Incentives Scheme*.

The ADE is the UK's leading decentralised energy advocate, focused on creating a more cost-effective, efficient and user-orientated energy system. The ADE has more than 100 members active across a range of technologies, and they include both the providers and the users of energy. Our members have particular expertise in combined heat and power, district heating networks and demand side energy services, including demand response. ADE members include owners and operators of CHP installations which range in size from 200 kW to 1.3 GW.

Consultation questions

Q1. Do you believe that the event submitted by NGET as an Income Adjusting Event constitutes an Income Adjusting Event?

- **Do you consider the proposed IAE to constitute force majeure as defined in the BSC or in the CUSC?**
- **Do you believe that the event submitted by NGET was unforeseen? Please provide evidence to support your view where possible.**
- **Do you believe that the proposed IAE costs were beyond the reasonable control of NGET?**

The ADE does not view the event submitted by NGET constitutes an IAE, as it is not an unforeseen event or circumstance. The market changes were completely foreseeable according to NGET's own Energy Futures Scenarios, as well as electricity and fuel market activity.

In 2012, NGET indicated expectation of station closures specifically in 2016, and that action would be needed to be taken to bring on new CCGT power plants, citing expected regulatory changes such as the European Large Combustion Plant Directive.

It is our understanding that when negotiating the conditions and budget for the 2015-2017 period a risk sharing factor was included as well as a mid-period budget review to give extra stability to NGET in what was considered at the time to be an unstable period. However, this instability was

covered by both the above tools and any risks, such as the obvious risk of coal stations exiting the market, should have been accounted for in NGET's budget. This is the approach and reasoning used by Ofgem when assessing NGET's IAE request in relation to the loss of 'Alcan' (a large frequency response provider) in the 2011-13 period, where the Authority found that NGET should have foreseen the loss of providers and should have had more robust alternative options.

In the Alcan scenario, it was known up to two years before the scheme in question that some providers (in the aluminium sector) were facing financial difficulties due to rising energy costs. This is a direct parallel with the current situation of coal plants providing BS capability. It is (and was acknowledged by NGET since at least 2012) a well-known fact that coal stations are facing financial difficulty and thus NGET should have been prepared for such a consequence.

From the above it is clear that at least from 2012 NGET foresaw changes to both the grid mix and its natural impact on procuring BS capability, which historically has only been from coal fired power stations. Not only was it clear to NGET that these events would take place in the immediate future, but NGET even specifically predicted that some stations would close by 2016.

In NGET's request for an IAE due to unforeseen Transmission losses in 2013, Ofgem responded that as NGET knew of potential market changes three months before signing the two-year scheme it could not then claim unforeseen events had occurred. In the present case, NGET's report was published four years before the alleged 'event' and can in no way be considered an unforeseen event.

Building on this point, oil and gas prices have been declining steadily for the past two years, increasing the competitiveness of gas generators at the expense of already (environmentally) burdened coal plants. If we consider the market conditions as well as Ofgem's own reasoning in its 2013 IAE decision, it is impossible to find that there was an 'unforeseen' event for the purposes of Special Licence Condition 4C.

Beyond Reasonable Control

In order to qualify for an IAE, NGET must not only prove that there were unforeseen events, but that the costs of these events were beyond the reasonable control of NGET.

It is our understanding that the costs incurred by NGET to obtain the services of Fiddler's Ferry and Drax were not beyond its reasonable control. As in the similar Transmission Losses IAE in 2013, NGET was, in this situation, best placed to forecast and control the impact of events that occurred during the 2015-2017 period.

We have been advised that NGET's prolonged inaction and overreliance on only one technology for BS capability resulted in awarding existing BS providers with an immensely powerful bargaining position over NGET. In the comparable 'Alcan' case where NGET claimed an IAE event had occurred, Ofgem stated that "NGET could have diversified its balancing services profile through contracting with other plant ahead of time, which could be considered appropriate given the cost impact of the risk of the smelter's closure materialising."

As mentioned above, NGET had the obligation to diversify in order to reduce the obvious risk that its traditional portfolio of providers was from a technology group that was being phased out of the market. An example of the consequences of this process is demonstrated in the price NGET paid to two generators for a one-year contract, an amount that is over 500% of the original 2015-2017 budget; a high cost consumers must bear.

It is clear that it would have been appropriate for NGET to, immediately after publishing its 2012 approach, run trials and supported upgrades to CCGTs and CHP units to ensure they were ready

for the predictable exit of several coal plants from the market. In both the NW and NE of England (where BS capability was procured in March) there are 27 CHPs and six CCGTs that could have contributed to BS capability at a much reduced cost.

To conclude, we believe that the proposed IAE costs were not beyond the reasonable control of NGET as it is clear that there were imminent market changes that would impact on its existing BS procurement strategy. It is our understanding that NGET knew of these changes and should have proactively sought to meet BS capability through a diversified set of technology providers, such as CHP and CCGTs, ideally through a competitive process, thus cowering costs for consumers.

In conclusion, the ADE does not view the event submitted by NGET constitutes an IAE, as it is not an unforeseen event or circumstance. On the basis of this conclusion Ofgem should reject the application for an IAE.

Q2. Assuming the event is an IAE, do you consider that any or all of the costs set out in NGET's notice were caused by the relevant IAE?

- **Are there any additional interactions between costs incurred that need to be taken into account?**
- **Do you consider that NGET acted economically and efficiently in procuring Black Start in this event?**

As discussed above, the ADE does not consider that the event is an IAE. However, there are further interactions that we would like to highlight even though much of the document has been redacted meaning it is difficult to identify which costs could in fact be an IAE and which are not.

The ADE does not believe that NGET acted in an efficient and economic way and it is unfortunate that Ofgem has decided to redact much of the information that would allow the public to scrutinise whether NGET acted appropriately in procuring BS capability, especially in relation to contract terms and bids from other parties.

We believe it would be appropriate for Ofgem to compare the new contracts with existing contracts to identify similar costs that would normally have been incurred. It is also our understanding that the timeframes around the procurement process were too short to allow any meaningful competition and that therefore the highest cost solution was procured.

Furthermore, Members have made us aware that this high cost solution has had a wider market impact. For example, on the day of the announcement, spark spreads for Winter 16/17 dropped by approximately £1/MWh, as a direct result of the contract and the fact that there would be higher levels of capacity available in Winter 16/17.

The ADE has significant concerns regarding these costs and the impact to consumers and wider energy market participants, and urges Ofgem to look closely at whether NGET has acted in an efficient and economic way.

For further information please contact:

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