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Wholesale Market Conduct
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Dear Marta,

Consultation on the Draft Transmission Constraint Licence Condition Guidance (the Consultation)

We are pleased to respond to the consultation on Ofgem's Draft Transmission Constraint Licence Condition (TCLC) Guidance.

In our response to Ofgem's consultation on the future of the TCLC in June 2016 we commented on the requirement for updated guidance to be published. Although the existing TCLC guidance (dated 29 October 2012) has served the industry well, we believe this is a timely opportunity to consider whether it can be improved.

A feature of the original guidance which we found particularly helpful was the examples of circumstances in which Ofgem might consider pricing conditions to be objectively justified (paragraphs 2.20-2.30 for Circumstance 1 and 2.38 for Circumstance 2), and the examples of indicators which Ofgem may consider when determining whether an excessive benefit has been obtained in Circumstance 2 (paragraph 2.36).

We are pleased that paragraphs 2.36 and 2.38 of the original guidance have been replicated in paragraphs 2.15 and 2.17 of the draft TCLC guidance, but would be disappointed if the helpful guidance relating to Circumstance 1 (found in paragraphs 2.22 to 2.30) was dropped as a result of these changes. We suggest that Ofgem consider issuing a new open letter (or an updated version of one of its existing REMIT open letters) to include these examples of objective justification relevant to Circumstance 1 in updated REMIT guidance. If Ofgem considers that the examples do not apply in the same way under REMIT, we would request that Ofgem uses such a new or updated open letter to explaining why this is its view and, also, give further explanation of how it will enforce REMIT in respect of behaviour currently dealt with as Circumstance 1 behaviour under the existing TCLC.

Ofgem may also wish to consider whether there are additional examples of objectively justifiable pricing decisions which can usefully be included in the guidance, based on experience and insights gained over the past four years. Based on our experience we would suggest:

- **Wider obligations including environmental and safety.** For example, hydro plants (conventional and pumped storage) face additional costs and/or operational constraints at times of high flood risk. In conditions of high rainfall or water level, it may be necessary to run the turbines and discharge water in order to protect the local community from environmental damage or safety hazards. In such circumstances, it should be objectively justifiable for operators of such plants to price BM bids in a way

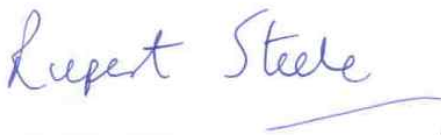
that reflects these risks (if they are capable of being costed) or in a way that seeks to ensure the unit is scheduled by the SO behind other available options available to it. Clearly it would be incumbent on the operator to continuously review and promptly revise prices in the event of changes in water management conditions. Similar environmental constraints may also apply to run-of-river hydro schemes in periods of drought, where there may be an environmental imperative to maintain water flow.

- **Ancillary service obligations.** In circumstances where operators have contracted with the SO for the provision of ancillary services and the provision of additional flexibility via BM instructions this may result in additional costs being incurred. It should, in our view, be seen as objectively justifiable for the operator to recover such opportunity costs via BM pricing.
- **Pumped storage opportunity costs.** If a pumped storage reservoir is close to capacity and the operator is obliged to pump following a BM bid acceptance, this may mean that the operator is unable to take advantage of lower GB-wide wholesale prices to pump later in the day, because the reservoir is already too full. To the extent that the operator can demonstrate a reasonable expectation of lower GB-wide prices, it should be objectively justifiable for the operator to recover such opportunity costs via BM pricing.
- **Imbalance costs.** In the event of a plant being dispatched off-load in the period prior to a system stress event but back on-load in time for the event, it should be considered objectively justifiable for the operator to recover costs which are statistically likely to be faced in the event of a failure to re-start in time to meet the event, via BM pricing.

Finally, we would query whether it remains appropriate to include 'contractual obligations' as a reason why pricing may be objectively justifiable. Whilst generators may have had contractual obligations to maximise renewable generation at the time TCLC was introduced, they will now have had sufficient time to renegotiate any such terms. In ScottishPower's case, we wrote in October 2012 to windfarms with which we had PPAs clarifying that any provisions in the PPA to maximise output should be considered as being subject to the requirements of TCLC. Retaining this example in the guidance could create a perverse incentive for windfarms to negotiate (or not renegotiate) terms which could then be used to justify what might otherwise be considered excessive pricing.

I hope you find these comments useful. Should you wish to discuss any of these points further then please do not hesitate to contact me.

Yours sincerely,



Rupert Steele
Director of Regulation