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27 March 2020

Dear Rachel,

Re: RIIO-GD2 NTS Exit Capacity Incentive

Thank you for the opportunity to provide respond to this consultation. We have set out our responses the specific question in the consultation in the attached appendix. NGN has provided detailed responses based on our experience of the RIIO-GD1 incentive and the CEPA consultation.

During the RIIO-GD1 period NGN has made considerable changes to our thinking and activities related to booking of NTS Exit Capacity. This has allowed us to use the incentive provided to reduce bookings while ensuring we are able to maintain our obligations to ensure sufficient capacity to meet our 1-in-20 obligations. This has freed up NTS Exit Capacity to be made available to other directly connected NTS customers located within our network footprint, and ultimately reduce costs for the consumer.

We believe that the current NTS Exit Capacity Review and changes to the NTS Exit Capacity Charging regime make it particularly difficult to suggest what a future incentive could look like without certainty of the operating regime. As a result we do not believe that there is value in either rolling forward the existing incentive regime or designing a new incentive regime. We do, however, believe that the RIIO-GD1 regime has created the appropriate behaviours at that it there is potential for a reputational incentive with a new RIIO-GD3 incentive being developed once the regime is more stable.

I hope these comments will be of assistance and please contact me should you require any further information in respect of this response.

Yours sincerely,

By email

Joanna Ferguson
Head of Market Services & Regulatory Compliance

Appendix1
Consultation Questions

Considerations for incentivising efficient NTS exit capacity bookings

1. *What specific GDN behaviours should any future exit capacity incentive mechanism seek to drive, and what consumer benefit would these deliver?*

   Any future incentive regarding Exit Capacity should encourage GDNs to make the minimum offtake bookings to enable them to meet their forecast 1 in 20 demand. GDNs should be encouraged not to hoard capacity when it's not needed. In addiction accurate bookings will signal more reliable requirements to the NTS.

   Taken together this should benefit consumers – by minimising the costs they ultimately pay through their bills. They will see lower more reflective Exit Capacity charges, and more accurate data should allow effective targeted asset investment only when it's needed, or indeed reduced asset costs should growth fall.

   The current incentive has worked well in reducing overall capacity bookings, and together with the Totex mechanism has encouraged more discussion with the NTS to ensure investment is targeted at the right assets. However we are now in a different position and the markets are changing, which means a new approach may be beneficial:

   - The current regime may be changing in RIIO-2 as a result of the ongoing consultation, which means setting an incentive now is difficult, given the rules may change significantly;
   - Potential increase in new large load connections associated with flexible generation may mean bookings and / or investments need to change;
   - During GD1 capacity has been significantly reduced to match current in 1 in 20 forecast demand. Any increase to bookings would be a result of changing localised demand, new connections, DESC CWV changes or operational strategy amendment. These changes should be allowed and encouraged as it allows capacity bookings to reflect demand and depicts a more accurate view of localised demand. User commitment under the current regime does not allow us to reduce capacity if demand decreases, therefore in some instance's bookings will not reflect the actual demand expected on a 1 in 20 peak day at the offtake level;
   - Where capacity below the baseline has been substituted by NTS to another customer, GDNs should not be penalised for taking their offtake bookings above the baseline when capacity requirements change, and an increase is needed. This will allow us to facilitate new connections, such as flexible generation sites and large loads connecting at the distribution level.

2. *Can you provide evidence of specific actions taken by GDNs in response to the RIIO-GD1 NTS exit capacity incentive, and set out how these have delivered lasting benefits to consumers?*

   In 2015 NGN undertook Risk Workshops to identify the opportunities and risks associated with significant reductions in our capacity bookings. As a result, we reduced our bookings from 612 GWh/day to 514 GWh/day over the course of GD1. This has been completed incrementally as and when user commitment has been satisfied. This has resulted in reduced capacity costs, albeit somewhat masked in price fluctuations and increases due to the current Charging

Regime. To illustrate the impact in reductions we have shown bill impacts using the 2013/14 prices: -

	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20
Bookings (GWh)	611.2	603.8	570.7	543.3	533.9	520.4	513.7
Cost at 13/14 prices (£m)	6.8	6.8	6.4	6.0	5.9	5.7	5.7

Following a review of operational strategy, we were unable to make significant changes to our booking strategy due to the geography and operability of our networks. Therefore, we were already at the best position and continuation of this strategy ensures the benefits are fully realised and enduring. A future incentive will encourage this review will take place periodically to ensure we are always in the best position as circumstances change.
Another benefit of reducing capacity on our LDZs has been freeing up our unsold Exit capacity for substitution by the NTS for large power stations. On our North East LDZ all our unsold capacity has been allocated to an NTS power station, allowing significant support to the electricity operator.

3. *Do you agree with the considerations we've identified, and the issues associated with them?*

- Exit Capacity Pricing – Agree. The validity of the current approach is in question when the charging model is set to change significantly in October 2020.
- Levels of spare capacity –Agree, however it is worth noting that we have seen an increase in our peak day forecast this year. With the connection of additional large loads this peak forecast might increase earlier than previously anticipated.
- Reward/Penalty calibration – Agree. As the charging model is based on a set level of income for the NTS with charges set to ensure recovery, there are no direct savings to our customers in the short term.
- Persistence of improvements – Agree. We expect the improvements we have made to be on an enduring basis, unless demand increases and we need to secure additional capacity.

4. *Are there any considerations, beyond those identified, that we should take into account for incentivising exit capacity bookings in RIIO-GD2?*

   Any changes implemented during the Capacity Access Review will need to be taken into consideration. For example, GDNs are working together to look at User Commitment and Substitution. User commitment is a significant issue which stops GDNs from reducing capacity when demand decreases, we believe this area needs improvement. With 'significant levels of spare capacity' on the NTS it brings into question the need for GDNs to book capacity on an enduring basis. Having the ability to match capacity with forecast demand would introduce more efficiency and reduce network capacity costs. We may see more localised growth and capacity requirements which could impact the operation of any incentive.

Options and Initial Thinking for RIIO-GD2

5. *Do you agree with the options CEPA has identified, and if not, what others should be consider for RIIO-GD2?*

   Yes we agree with options presented. NGN would support a reputational incentive in GD2 and encourage Ofgem to be open to a new incentive structure in GD3 when the improvements to the regime via the Capacity Access Review are in place

6. *Which of the options presented by CEPA is your preference for RIIO-GD2 and why?*

   As mentioned under Q1, NGN believe the GD1 Exit Capacity Incentive has successfully achieved its attempt to encourage GDNs to minimise the cost of booking sufficient NTS exit capacity to meet their 1-in-20 peak demand obligations. The incentive has driven the right behaviour, price signals and operational efficiency under the current Exit Capacity Regime. Moving forward into GD2, we do not feel that the current incentive structure provides us with further opportunities to drive more consumer benefit. Furthermore, it does not make sense to develop an incentive when the ongoing Capacity Access Review will lead to significant changes in the Exit Regime. NGN would support a reputational incentive in GD2 and encourage Ofgem to be open to a new incentive structure in GD3 when the improvements to the regime via the Capacity Access Review are in place.

7. *If we removed the existing incentive mechanism without any mitigations, what are the potential risks and how should these be managed?*

   The risk would be that GDNs change the behaviour that the GD1 incentive has encouraged in relation to releasing unused capacity back to the NTS. A reputational incentive which would see networks reporting on and explaining any capacity changes would go some way in alleviating this risk. Continued discussions with NTS regarding investments decisions and potential trade-offs should be encouraged. An example being a reduction in our agreed offtake assured pressure to save NTS compressor costs.

8. *If we remove the existing incentive mechanism, what enhanced obligations could we consider introducing for RIIO-GD2 that would effectively maintain GD2 booking restraint? Please provide any specific examples.*

   An Annual Report detailing capacity changes and the reasons behind them.