ENGIE Profile

ENGIE, formerly known as GDF SUEZ, is a global energy company present in 70 countries worldwide operating in four key sectors of power, natural gas, renewable energy and energy services. The company puts responsible growth at the heart of all its businesses in order to address major energy and environmental challenges: responding to the demand for energy, ensuring security of supply, combating climate change and making optimum use of resources.

In the UK, ENGIE has interests in a number of activities across the energy value chain, from gas exploration and production through to services. In total, ENGIE employs approximately 17,000 people throughout the UK across all of its businesses. In generation, ENGIE is one of the country's largest independent power producers, with interests in 4,025 MW of plant. This comprises a mixed portfolio of generation assets that include gas, CHP, wind and the UK's foremost pumped storage facility. ENGIE also operates a major energy retail business supplying electricity and gas to the Industrial and Commercial sector, and is entering the domestic retail market in 2017.

ENGIE is also the UK's leading district energy company. We design, build, finance and operate district heating schemes on long term concession agreements. ENGIE's high profile district heating schemes include; the Queen Elizabeth II Olympic Park, Southampton District heating scheme, Whitehall District Heating scheme, Leicester District Heating Scheme and Birmingham District Heating Scheme.

Outside of energy, ENGIE is a leading services provider to the public and private sector in the UK, delivering a wide range of facilities management and back office services.

ENGIE welcomes the opportunity to respond to Ofgem's consultation on Initial Proposals for electricity SO incentives from April 2017

Summary

- Ofgem recognises that information asymmetry exists in the BSIS model methodologies. ENGIE therefore welcomes the proposal for an independent audit. The appointment of a suitably qualified auditor, independent from any financial auditor, will help to ensure that a suitable target is set and reduce the opportunity for NGET to readily hit its incentive cap.

- The incentive scheme is highly complex and this consultation has demonstrated the shortcomings in both the model used to forecast BSIS cost and also in explaining why, even after errors have been addressed, it is still not possible to identify the cause of model outperformance. It will be extremely important that the independent auditor can demonstrate that it is fully able to challenge the assumptions that are being made by NGET in setting out its proposals.

- Given the lack of time to develop an alternative scheme, for the 2017, ENGIE welcomes the intention to reduce the cap and floor and the sharing target and to rectify model errors within a short timescale.

- Going forward, ENGIE believes that rather than adding more layers of complexity to the current incentive scheme, Ofgem needs to start with a 'blank sheet of paper' in its longer term review. The errors in 2015/16 and 2016/17 coupled with unexplainable model outperformance suggest that the current approach is no longer fit for purpose. ENGIE's preferred approach is to end the

incentive scheme and replace it with a much stronger enforcement of the licence obligation on National Grid to procure and despatch balancing services in an economic and efficient way. To provide assurance of this, Ofgem should consider "embedding" its staff or technical experts in the SO to ensure that best value for customer is obtained in all time scales.

- ENGIE supports the changes to the C16 licence condition which will place a requirement on National Grid to take the most efficient actions to balance the system, including the cost of contracting with a provider outside the Balancing Mechanism (BM) versus within the BM. ENGIE has already raised BSC modification P354 to remove the spill payment associated with the delivery of non BM STOR from the supplier's account. The mechanism to address this C16 requirement for non BM spill payments is therefore in play. ENGIE sees P354 as a precursor to the introduction of a BM 'lite' level of participation. For National Grid to comply with this new licence condition, implementation of P354 should not be delayed in order to deliver a full BM 'lite' solution.

- ENGIE agrees that it is appropriate to remove Black Start capability costs from BSIS. Black start warming costs are now significant and should remain in BSIS. ENGIE also agrees that National Grid should be required to set out an approved strategy and procurement methodology. With the traditional coal providers of black start (coal plant) set to close by 2025, a long term view of requirement is needed and this should be a key focus of the black start strategy.

Other points

- ENGIE expresses concern that what seem to be fairly minor errors (a typographical error in one constraint boundary, errors on the simulation of the dispatch of biomass in the market, as well as some errors on its approximation of Solar PV location in the South East and on some constraints boundaries from the year-ahead outage plan) have resulted in a reduction in the BSIS target for 2016/17 of £491m.

- In 2015/16, NGET incurred costs of £868million compared to a target of £1,082million, resulting in NGET hitting the BSIS incentive cap. ENGIE is surprised that Ofgem does not intend to change the mechanism that allows for corrections of past incentive scheme performance (paragraph 2.4.1). Given the errors in the 2016/17 scheme, ENGIE believes that the 2015/16 scheme should be re-opened to establish the reasons for the disparity between the target and outturn costs. Any incentive payments arising from these errors should then be clawed back.

- Ofgem, in its decision letter on the black start Income Adjusting Event, said:

  "During the process of assessing the IAE request several issues were brought to our attention. These relate to, among others, compliance with REMIT; potential competition law issues; alleged deficiencies in the long term Black Start policy; and national and regional security of supply concerns. The Authority also notes that industry code modifications have been raised in relation to IAEs. The Authority's focus has been on assessing the IAE as thoroughly as possible in the three month period available and the Authority has not yet made any decisions on these other issues. The Authority will fully explore these issues and take any appropriate action.

- ENGIE believes that whilst this consultation has started to address the deficiencies in the black start policy, it should also look at the competition issues that were raised by respondents to the consultation. These do still need to be addressed to ensure that future procurement complies with competition law and REMIT declarations.

Responses to consultation questions

CHAPTER: Two	
Question 1: Do you agree with our proposals to introduce new licence requirements / guidance around SO balancing behaviour? **Question 2: Do you agree with the clarifications we propose to introduce to NGET's licence? Is there anything missing or that should be removed?**	The C16 licence conditions place obligations on National Grid (NG) to procure and despatch balancing services in an economic and efficient way. ENGIE agrees with Ofgem that this is the most important area for regulation and sets the background to much of the System Operator (SO) actions in this area. However, ENGIE has two concerns with the current obligation. Firstly, in some circumstances they are seen by the SO as a set of guidelines rather than licence conditions, and when challenged on the application of the conditions the SO has the ability to trade off short term costs against projected long term benefits. The SO makes a judgement call on the type and volume of services required in future years. In the past this has led to an over emphasis on the procurement and development of new services that has ultimately led to significant short term costs as existing providers exit the market early. Secondly, the enforcement of any breach of the conditions is problematic. Only Ofgem can hold the SO to account for breach of the licence conditions and take enforcement actions, but this is seen as an extreme option and is unlikely to be used for any but the most serious breaches. In this context, ENGIE supports the clarification of the licence conditions but believes that the short term operation of the system should instead be covered by a specific obligation relating to minimising the total cost to the consumer of balancing the system both on the day and within month. This will ensure that customers get good value for money in the short term and are not in the position of subsidising future customers. A further licence condition is needed that would allow any licenced party to raise concerns as to the application of the licence conditions, and have these considered by the SO in the first instance with an obligation to provide appropriate justification. It may be prudent for Ofgem to consider ensuring that the SO use an external panel of "technical experts" from the industry who have the skills to hold the SO to account over C16 licence conditions as part of this process. Via the BSC Modification process, ENGIE has already raised a specific issue relating to the use of non-BM plant and the resulting cost of imbalance energy. A useful C16 clarification would be that the overall cost of balancing services must include all costs resulting from SO actions and not just those that feed into BSUoS.

	Going forward, ENGIE believes that regulation through the transparency of actions against licence conditions is likely to be a better model for the consumer than the current incentivised approach. Without an incentive scheme, more oversight of the SO's balancing activity will be needed. We would encourage Ofgem to consider "embedding" staff or technical experts in the SO to ensure that best value for the customer is obtained in all time scales. In addition, third parties should be able to challenge NG's actions. Both of these should be viewed as routine and positive ways to improve SO performance.
Question 3: Do you agree with our Initial Proposal of maintaining a model-based target from April 2017 until March 2018?	With little time to develop an alternative, from a practical perspective ENGIE supports this approach although with a significantly reduced target as has been proposed. It is clear that whilst the BSIS does put commercial pressure on the SO to reduce costs, the real effect of this is small and the use of Income Adjusting Events (IAEs) when additional unforeseen costs occur simply undermines the scheme.
Question 4: Do you agree with our proposed changes to the governance and incentive parameters? Is there anything missing or that should be removed? Please explain your answer.	ENGIE supports this approach but believes that non-BM spill energy payments need to be explicitly included in BSIS costs. ENGIE's BSC modification P354 will provide the opportunity to achieve this.

CHAPTER: Three	
Question 1: Do you agree with our proposal to remove Black Start from BSIS?	ENGIE supports this approach. ENGIE believes that the capability of the service should not be part of an incentive scheme. There is merit in keeping the associated "warming costs" within the incentive scheme.
Question 2: Do you agree with the principles of our Black Start regulation? Should we add or remove any principle? Please explain your answer.	Black start as a key system service has two main costs; the cost to provide the capacity for the services (fuel system, diesels engines /OCGT and integration into the larger station) and the cost to ensure the short term (a few hours) availability of the service by keeping the units warm. We believe that the procurement of new black start capability should be on a "cost plus basis" with the SO selecting the most economic option being mindful of the fuel source of the services. This should ensure that most new, large (over 1000 MW) stations are built with this capability. Warming payments are increasing given the changing dispatch profile of thermal assets. The costs are now significant and it is appropriate that warming payments remain within the 2017 BSIS. ENGIE believes there is also a wider role for the SO and Ofgem in reviewing the requirement and how it can be met with fewer

	large thermal units. There may be the case for funding small "Black Start only" OCGT plant at strategic locations to secure the system. This may be a cheaper option compared with continuous warming of thermal units.
Question 3: Do you agree with our proposed regulatory framework for 2017/18? Please explain your answer.	See above.

CHAPTER: Four	
Question 1: Do you agree with our amended wind generation forecast incentive proposal? Are there any elements you feel should be changed or that are more relevant to you? Please explain your answer.	ENGIE does not believe there should be any additional incentives. The current scheme should be allowed to run on for a further 12 months without any explicit additional services or changes to parameters other than to reduce the maximum benefit. The scheme should ultimately be replaced with licence obligations, transparency and independent assessment of SO actions.
Question 2: Do you agree with our proposal to introduce demand forecasting incentives in this interim scheme? Are there any elements you feel should be changed or that is more relevant to you? Please explain your answer.	Please see above answer to Chapter 4, Question 1.
Question 3: Do you have any additional criteria that you would propose for the Quarterly Forecast Report? Please explain your answer.	Please see above answer to Chapter 4, Question 1.
Question 4: Do you agree with how the parameters for the incentives are calculated? Should we consider anything else when setting the target?	Please see above answer to Chapter 4, Question 1.
Question 5: Do you believe we should introduce an additional mechanism to counter the incentive to under or over-forecast in any given month to maximise incentive value? Please explain your answer	Please see above answer to Chapter 4, Question 1.

CHAPTER: Five	

Question 1: Do you agree with our proposal to introduce a mechanism for the SO-TO to exchange funds? Please explain your answer.	ENGIE does not agree that there is a need for a SO-TO incentive. One of the benefits of common ownership of the SO and the onshore TO is the close co-operation that exists between the two areas. We believe that the existing licence requirement to co-ordinate the activities is sufficient. The existing TO RIIO settlement provides sufficient funds to meet the licence requirement. Were there to be an independent SO, it would be appropriate for this type of incentive to be put in place.
Question 2: Do you agree with our proposal to introduce a pilot SO-TO incentive? Do you agree with the structure proposed? Is there anything missing or that should be removed? Please explain your answer.	Please see above answer to Chapter 5, Question 1.
Question 3: Do you agree with our proposal to introduce a requirement for a quarterly report? Is there anything missing or that should be removed? Please explain your answer	Please see above answer to Chapter 5, Question 1.

CHAPTER: Six	
Question 1: Do you agree that the proposed changes described in Chapter 2 will enhance transparency?	ENGIE believes that transparency and the ability to challenge SO actions in a controlled way will be key to regulating the SO going forward. The key areas for concern are: • There is a low level of transparency of SO actions relating to the demand side. Whilst BM actions are visible to the market in real time, no information is available on the use and despatch of the demand /non-BM side of the market. • The SO has moved many services onto standard tendered terms and ENGIE supports this approach as it does increase transparency. ENGIE believes that these standard products should also include delivery reports where specific contracted parties (aggregators/ BM units and non BM units etc.) have their ability to deliver reported. This is a key opportunity to improve performance of all providers. Some of the suggested transparency reports will address these concerns but these may need to be part of a further review of SO information provision including whether "self-certification" of the delivery of some services remains appropriate.
Question 2: Do you agree with our proposal to not introduce a	No – ENGIE believes there should be no new financial incentives

financial incentive on transparency? Please explain your answer.	
Question 3: Do you agree with our proposal to retain the MDLC? If not, please explain your answer.	No – ENGIE believes there should be no new financial incentives
Question 4: Do you agree that we should amend the MDLC to require NGET to get third party scrutiny on areas where the model could be improved? Please explain your answer.	No – ENGIE believes there should be no new financial incentives
Question 5: Do you agree with our proposal to discontinue the System Operator Innovation Roll-Out Mechanism? Please explain your answer.	Yes – ENGIE agrees with the proposal.

For further information, please contact either:

Libby Glazebrook
Policy Advisor
Tel 0207 320 8805
libby.glazebrook@engie.com

Simon Lord
Director – Transmission Services
Tel 01352 705289
simon.lord@engie.com