

**Malcolm Arthur**  
NGET  
Grid House  
Warwick Technology Park  
Gallows Hill  
Warwick  
CV34 6DA

Telephone: 01738 457377

E:mail: garth.graham@  
scottish-southern.co.uk

Our Reference:

Your Reference:

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Dear Malcolm,

### **NGET System Operator Incentives for 1 April 2010[Part 1]: issued 4 August 2009**

Thank you for the opportunity to respond to the above consultation and for allowing us a short extension to the deadline.

We have reviewed the document and provide our comments to the questions posed below, and we look forward to responding to the subsequent consultations in due course.

*1 What benefits do you see for the development of an indexation methodology for reactive power costs? What drivers should be included in such an index?*

As noted in the consultation, indexation removes some of the risks of windfall gains and losses that are out-with the control of NGET. In principle therefore indexation should be pursued where practical. For the current scheme, NGET consulted on potential indexation and proposed a Power Price index be included. However, this was not accepted by Ofgem. It is clear therefore that the case remains to be made and that more information needs to be provided on the correlation between the cost drivers and outturn costs and the impact these drivers have on outturn costs before any indexation could be put in place.

*2 What benefits do you believe there are in the implementation of a longer than one year scheme?*

In principle we favour longer-term schemes, and given the relative stability of the Reactive Power costs, it seems appropriate that a longer-term scheme is considered. We agree that longer-term schemes could incentivise other third party providers of Reactive Services to enter the market. However it is not clear whether Reactive Power can be suitably unbundled to allow a longer-term scheme for Reactive Power to be put in place.

*3 Are there any additional benefits or drawbacks in the development and implementation of an unbundled reactive power incentive?*

In principle, we favour unbundled schemes where this is possible. However, Reactive Power requirements are driven by power flows, as are other elements of BSIS, e.g. Transmission Losses and it is clear that for the current scheme, the case was not sufficiently made for unbundling. Further information on this interaction and the effect of unbundling is required before Reactive Power could be suitably unbundled.

*4 Please provide your views on the development of the reactive power incentive? Do you see any benefits in changing the current arrangements?*

We can see benefits in creating a longer-term incentive for Reactive Power however the case for unbundling needs to first be made.

*5 What benefits do you see for the development of an indexation methodology for transmission losses? What drivers should be included in such an index?*

Again, we agree that indexation should be pursued where practical. However, given the current form of the incentive scheme, based on volumes, we are not clear that there is a practical indexation. Whilst the deadband reflects the uncertainty of generation patterns, we do not believe that a suitable index could be formulated that would allow the need for a deadband to be reviewed.

*6 Please provide your views on whether the SO can influence sufficient drivers to reduce Transmission Losses?*

The SO is able to influence the dispatch of plant through the Balancing Mechanism and its contracting with generators and it would be expected that this is done on an economic basis. Whilst this influence may be relatively small, it is greater than the level in the BM portrayed in the consultation. It also has to be balanced against the inevitable disposition of renewable generation, that is likely only going to exacerbate constraints.

*7 What benefits do you believe there are in the implementation of a longer than one year scheme?*

A longer-term scheme could be of benefit to the SO in terms of longer-term improvements to IT systems to manage constraints.

*8 Are there any additional benefits or drawbacks in the development and implementation of an unbundled transmission losses incentive?*

Again, in principle we favour unbundled schemes. However, as with Reactive Power, Transmission Losses is dependent on power flows. It is not clear therefore that it can be effectively unbundled.

*9 Please provide your views on the development of the transmission losses incentive? Do you see any benefits in changing the current arrangements?*

Based on the assumption that transmission losses cannot be unbundled, it is not clear that there is a great deal of latitude to change the form of the incentive scheme on losses.

*9b Are there any benefits in the development of a TO incentive to manage fixed losses?*

No. We do not believe that there are any practical solutions that can be carried out by the TO that would enhance the requirement they already have on them to consider the procurement of low loss equipment. The scale of the equipment and chunkiness of its installation would not lend itself well to an incentive scheme.

*10 What benefit do you see in developing a transmission losses zonal forecast incentive?*

If, a zonal losses modification is implemented, via the BSC, then it may be appropriate to consider such a forecast after that. However, at this stage it would not be efficient to pursue.

*11 What benefit do you see in the development of a Transmission Losses procurement incentive similar to the Gas Shrinkage incentive?*

We do not believe that NGET have the same influence over the whole of transmission losses as they do in gas, and therefore do not believe that it would be appropriate to have them responsible for the whole of the 6TWh of losses.

*12 Do you agree that National Grid should be incentivised on the procurement of black start services for 2010/11 and 2011/12 as under the current scheme framework?*

Yes.

*13 Do you believe that the black start scheme should be extended to a 2 year target?*

Given the costs for the next two years are reasonably certain, it seems appropriate that the scheme is extended to two years, though given that certainty, the incentive scheme should be tightly defined.

*14 How do you believe black start services are best procured post 2012?*

We agree that a review of the procurement of Black Start services post 2012 is required. However, it needs to be based on a technical appraisal, based on the LJRPs, of the requirements for Black Start services going forward.

*15 Did you find the level of information within this consultation informative? What additional information should National Grid provide to explain better?*

For this stage of the consultation, the level of information was adequate. It could be improved by including comparisons with previous years' incentive schemes, and also the policy background from previous years, e.g. highlighting the consultation on Indexation last year and the outcomes. This would inform the present consultation, and perhaps save going over old ground.

*16 Do you have any further comments on any aspect of this consultation in relation to the Electricity SO?*

No.

We hope the above comments are helpful to you in your deliberations.

Yours sincerely

Garth Graham  
Electricity Market Development Manager  
Energy Strategy