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Dear Malcolm,

**National Grid Electricity Transmission System Operator Incentives for 1 April 2010
(Mini Consultation 3)**

Thank you for the opportunity to respond to the above mini consultation. This response is made on behalf of E.ON UK plc.

Our answers to the specific questions raised in the consultation are as follows:

1. Do you believe that the drivers for the volume of generation have been identified? How much control do you believe National Grid has on volumes?

These would appear to have been adequately identified and described.

- 2. Have all cost drivers been captured and correctly identified as being within or outside National Grid control?**
- 3. Do you consider that there are elements within these cost drivers that are within National Grid control? What are these and how do you believe these should be considered in the future?**

They do appear largely to have been adequately identified. It may be true to assert that National Grid as the System Operator has limited control over some of these items. However, to absolve National Grid as an organisation of all influence over system faults for example would seem to be inaccurate. Presumably the amount of maintenance on the

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transmission system has an impact on its resilience to faults. Also the effects of faults once they occur can be affected by the design and operation of the system.

Similarly, whilst the bid offer spread is not in the direct control of National Grid, the extent to which National Grid utilises the Balancing Mechanism in order to address constraints is under its control. Therefore, National Grid has some influence on what impact a particular spread has on costs.

4. To what extent do you believe that the increase in connected generation behind non compliant boundaries due to Interim Connect and Manage will impact constraint costs and as such is a key driver?

We believe that without any mitigating action then Interim Connect and Manage has the potential to increase constraint costs to a significant extent. Clearly the debate as to the best measures to put in place is taking place in a different forum. However, it is valid to consider Interim Connect and Manage as a potential key driver of constraint costs.

5. To what extent do you believe the increase in wind generation will impact constraint costs and as such is a key driver?

Clearly, as wind generation has very low avoidable costs and may be seeking to recover lost ROC revenue, constraining it off is likely to be more expensive than doing so for conventional plant. The exact extent to which this is likely to happen into the future is not something on which we have a view at present. Any analysis that National Grid has done or knows is available from elsewhere would be very useful.

6. Do you agree the drivers for constraint costs are significantly different from those of other components of system operation?

We are uncertain that this is indeed the case, or at least sufficiently so as to warrant an unbundled scheme. Indeed market length and market prices appear to have a bearing on the effects of constraints in terms of volumes and costs. We would expect them to have a bearing on other elements of costs too. The choice of plant that National Grid uses for other services such as for holding reserve will have an effect on the distribution of plant on the system which affects the potential for constraints.

7. Are there any additional benefits or drawbacks in the development and implementation of an unbundled incentive?

In our response to the previous mini consultation we noted that one of the important considerations in setting the scheme is the amount of interactions between various elements that make up balancing services. Past discussions regarding cash out prices show for example that there is an interaction between the actions taken for constraint purposes and those taken for energy balancing. Often it can be shown that actions are taken for both purposes. More fundamentally, however, it is clear that it is not possible to define precisely what is energy and system balancing.

Therefore, given the interactions between different elements of balancing costs and the

difficulty to allocate certain actions to each category, we believe that any unbundling of costs should be kept to a minimum. Therefore, we are supportive of maintaining a bundled scheme.

8. Please provide your views on the methodologies described? Is there an alternative methodology which should be developed?

We do not have a preferred methodology and would prefer to see no unbundling.

9. Do you agree that it would be appropriate to have an adjustment term to mitigate National Grid's exposure to uncontrollable and unpredictable risks affecting constraint costs?

We do not believe that this would be productive. If we take each issue raised in the consultation in turn:

Bid/offer spread – as we mention above, although National Grid may have little direct involvement in the bid/offer spread it does make choices as to the extent to which it uses the Balancing Mechanism to address constraints. Therefore, the cost implications are to some extent controllable.

Volume of new generation connecting – this seems only to be particularly problematic if you make the scheme longer than one year. It would be interesting to see statistics as to the extent that assumptions about plant connecting at the year stage ahead turn out to be incorrect during the year concerned. However, this appears to be a relatively manageable issue.

Volume of generation behind derogated boundaries – this would seem to be a subset of the new volume of generation connecting and subject to the same risks.

Number of outage weeks on planning boundaries – we believe that to remove an incentive on this element is inappropriate for similar reasons outlined in paragraph 181 of the document, namely that it would remove the incentive on the SO to seek reductions with the TOs of the number of weeks an outage is required for, or its impacts when it is active.

10. What items that you believe it would be appropriate for any adjustment term to cover and how would these work?

We do not support such an adjustment.

11. Please provide your views on the development of an alternative method to manage constraint costs due to fault outages? Is there an additional method which should be developed?

As we mention above, we believe that there are actions that National Grid can undertake that affect the likelihood of faults on the system. We believe that undermining the incentives to do so would be inappropriate.

12. Do you agree that development of an alternative treatment for fault outages is appropriate?

No.

13. Do you believe there are benefits in the implementation of a longer than one year scheme? Please describe your views on the optimal incentive duration for constraints.

As with our response to previous consultations, we do not believe that a scheme of over one year would be appropriate as it increases the likelihood of Income Adjusting Events which are a significant risk to BSUoS payers.

14. Do you have any comments regarding this consultation process?- Document structure - Overall content and level of information provided – Process

We have nothing further to add.

I hope the above comments prove helpful.

Yours sincerely,

Paul Jones
Trading Arrangements