

Peter Bingham
National Grid

Cc: Ofgem

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Via email

Dear Peter

Re: Demand Side Balancing Reserve and Supplemental Balancing Reserve: Final Proposals Consultation

Thank you for the opportunity to respond to your consultation. Our response reflects the views of the Centrica group of companies excluding Centrica Storage.

Further Centrica views on accelerating the Capacity Market and increasing STOR volumes as alternatives to SBR

An accelerated Capacity Market (CM) would be the best way to address concerns about Loss of Load Expectation in mid-decade winters. However, we note DECC's view that this option is impractical and we recognise the CM is not a matter for National Grid.

We note your view that increasing STOR volumes has potential disadvantages over SBR. For example, STOR plant would not be restricted from participating in the market outside availability windows and there may be less surety for National Grid around STOR megawatts being genuinely additional. However, the ability of STOR to respond rapidly to an SO instruction is highly desirable in the context of providing genuine last resort reserve. From the point of view of minimising market distortions, the later the SO is able to defer an instruction, the better. We therefore recommend that SBR candidates with faster response times should be evaluated more favourably than slow response candidates in any future SBR tender (see below).

Centrica recommendations on SBR

If National Grid decides to submit SBR proposals to Ofgem, and ultimately procure SBR, we recommend that the following provisions are made, to minimise the risk of undesirable consequences:

1. The SBR service should expire when Capacity Obligations commence via the CM – this should be expressly set out in the Balancing Principles Statement. If the first capacity auction is not held by the end of Q1 2015, there should be a re-consultation exercise on any extension of SBR.
2. In Q1 2014 (and Q1 of each subsequent year) National Grid should publish an assessment of whether probability weighted LOLE exceeds 3 hours per year for 2014/15 and the following 2 years (or the relevant years for later statements). If LOLE does not exceed 3 hours per year, the system is meeting DECC's reliability standard and National Grid should cancel its planned SBR tender for that year.
3. SBR tenders should be rejected if bids fail to meet your proposed criterion: *Value of Lost Load (VoLL) x Reduction in Expected Energy Unserved > Cost of SBR bid.*
4. SBR tenders should be ranked mainly on price, but National Grid should give weight in its tender evaluation to SBR megawatts capable of responding rapidly to an SO instruction. The value of megawatts with shorter response times should be recognised in any SBR tender, as this will help minimise market distortions.
5. SBR tenders should admit *parts* of plant otherwise unavailable to the market as well as whole plant (e.g. a steam turbine on a CCGT should be admissible where the Gas Turbine is available to the market but the steam turbine is not). This will facilitate procurement of the required SBR megawatts at least cost.

Centrica recommendations on DSBR

1. The DSBR service should expire when Capacity Obligations commence via the CM – this should be expressly set out in the Balancing Principles Statement.
2. National Grid should remove (or reduce) their default price bands for DSBR, to avoid the risk of overpaying for the DSBR service. DSBR bidders should be able to bid at below £1000/MWh if they are willing to.
3. National Grid should ensure suppliers are properly consulted at the DSBR pre-marketing phase – this will facilitate supplier led DSBR aggregation and help simplify National Grid's DSBR contracting arrangements.
4. We agree that the DSBR set up payment should be recoverable if DSBR units fail to meet their demand reduction obligations.

Our responses to your specific questions are appended below. Please contact me if you would like to discuss our response further.

Yours sincerely,

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DSBR Questions

Q1. Do you consider that the proposed amendments to the DSBR product sufficiently address the issues raised in the consultation?

We **support** your proposal to recover the £10/KW set up fee in the event DSBR resources fail to deliver demand reduction.

We **support** the requirement for DSBR resources below 1MW to participate via aggregators and/or suppliers. We would underscore the value of supplier engagement in your proposed DSBR pre-marketing phase to facilitate this.

We **do not support** the use of default price bands for DSBR resources; particularly given the lowest price band is £1000/MWh. We believe DSBR resources should be able to bid at lower rates if they are willing to.

Q2. Do you support us taking forward the DSBR product with these amendments?

The proposed DSBR service is acceptable subject to our comments in our cover letter and in our answer to question 1.

We believe DSBR should expire when Capacity Obligations commence via the CM. As the DSR pilot phase of the CM ramps up between 2015 and 2018, there should be a corresponding ramping down of DSBR. The CM should be the enduring instrument for security of supply in GB for both generation and demand reduction services.

SBR Questions

Q3. Do you consider that the proposed the amendments to the SBR product sufficiently address the issues raised in the consultation? Do you consider that the additionality provisions discussed in Section 5 are sufficiently robust, or whether these should be reinforced?

We recognise there are challenges around additionality for SBR.

We **agree** with your proposed requirement for a Board declaration that any megawatts bid into SBR would be otherwise unavailable to the market. This is a simpler and less subjective way for National Grid to validate SBR tenders against their additionality requirement than other measures, such as requiring economic analysis of a plant's unviability to be submitted.

We query whether it is practicable and do not think it is reasonable to enforce declarations of non-availability from any megawatts rejected in an SBR tender, as National Grid would have no contract with the unsuccessful SBR applicants. Hence we **do not support** further measures to ensure additionality (such as a market re-entry fee). If a party following a tender rejection decides to incur the significant costs of mothballing a unit rather than closing it then they should have the commercial freedom to utilise the unit as they wish. This can only be in

consumers' interests.

Q4. Do you agree that procuring large volumes of extra STOR would be less economic and cause more distortion to the energy and balancing markets compared to SBR?

We acknowledge that STOR units would not be restricted from participating in the market outside availability windows and that there may be less surety for National Grid around STOR megawatts being genuinely additional. We do however believe that the ability of STOR to respond rapidly to an SO instruction is highly desirable in the context of providing genuine last resort reserve. From the point of view of minimising market distortions, the later the SO is able to defer an instruction, the better.

We therefore **recommend** that SBR tenders should be ranked mainly on price, but National Grid should give weight in its tender evaluation to SBR megawatts capable of responding rapidly to an SO instruction. The value of megawatts with shorter response times should be recognised in any SBR tender. If prospective SBR units incur costs in remaining available to meet a defined response time, these should be built into their tender price.

Q5. Do you support us taking forward the SBR product? If not, what would be your recommended course of action if margin outlook deteriorates over the next 12 months?

We accept there is a case for continuing to assess LOLE in the mid-decade winters, given DECC's proposed 3 hrs /yr reliability standard. We are equally mindful of the need to minimise the cost to consumers of measures to reduce LOLE.

Any procurement of SBR must be done on a strict value basis, minimise market distortions to the greatest possible extent and expire once Capacity Obligations commence via the CM.

To reiterate from our cover letter, our **recommended conditions for procuring SBR** are as follows:

1. The SBR service should expire when Capacity Obligations commence via the CM – this should be expressly set out in the Balancing Principles Statement. If the first capacity auction is not held by the end of Q1 2015, there should be a re-consultation exercise on any extension of SBR.
2. In Q1 2014 (and Q1 of each subsequent year) National Grid should publish an assessment of whether probability weighted LOLE exceeds 3 hours per year for 2014/15 and the following 2 years (or the relevant years for later statements). If LOLE does not exceed 3 hours per year, the system is meeting DECC's reliability standard and National Grid should cancel its planned SBR tender for that year.
3. SBR tenders should be rejected if bids fail to meet your proposed criterion: *Value of Lost Load (VoLL) x Reduction in Expected Energy Unserved > Cost of SBR bid.*

4. SBR tenders should be ranked mainly on price, but National Grid should give weight in its tender evaluation to SBR megawatts capable of responding rapidly to an SO instruction. The value of megawatts with shorter response times should be recognised in any SBR tender, as this will help minimise market distortions.
5. SBR tenders should admit *parts* of plant otherwise unavailable to the market as well as whole plant (e.g. a steam turbine on a CCGT should be admissible where the Gas Turbine is available to the market but the steam turbine is not). This will facilitate procurement of the required SBR megawatts at least cost.

Costs & Funding Questions

Q6. Do you agree that our cost estimates, and the underlying assumptions, are reasonable?

We **agree** that your STOR based cost estimates for SBR appear reasonable (~£25/KW), although we note the cost of SBR megawatts could vary significantly from case to case. We would expect the cost of returning a retired plant to service to be higher than keeping existing megawatts on the system that were at risk of retirement, for example.

Q7. Do you agree that it would be inappropriate to include these costs in the Balancing Services Incentive Scheme until such a time prices and volumes for these products are better understood?

We acknowledge your rationale for SBR being outside BSIS. However, if the costs are outside BSIS, it is all the more important that National Grid accepts SBR tenders on a strict value basis, as proposed in your first SBR consultation.

Our recommended conditions 1, 2, 3 and 5 for any procurement of the SBR service should ensure that costs are appropriately controlled:

1. The SBR service should expire when Capacity Obligations commence via the CM – this should be expressly set out in the Balancing Principles Statement. If the first capacity auction is not held by the end of Q1 2015, there should be a re-consultation exercise on any extension of SBR.
2. In Q1 2014 (and Q1 of each subsequent year) National Grid should publish an assessment of whether probability weighted LOLE exceeds 3 hours per year for 2014/15 and the following 2 years (or the relevant years for later statements). If LOLE does not exceed 3 hours per year, the system is meeting DECC's reliability standard and National Grid should cancel its planned SBR tender for that year.
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Q8. Do you agree with the proposed approach to the recovery of incremental internal costs we would incur if we were to procure these additional balancing tools?

We **accept** your proposed approach to recover incremental internal costs. We underscore the importance of minimising internal costs associated with SBR and DSBR.

Further Centrica comment – transparency on SBR procurement and dispatch

We support National Grid being as transparent as possible in its assessment of the case for procuring SBR in mid-decade winters.

In the event that SBR is procured, we also believe it is important to dispatch it as transparently as possible. We favour SBR dispatch within the Balancing Mechanism (BM), subject to SBR being a last resort option that is not dispatched ahead of regular BM plant, regardless of utilisation price. We believe a system of flagging SBR plant would be one way to ensure transparent dispatch to the market. We would also support the development by National Grid of appropriate system warnings, so the market was aware of any SBR dispatch instructions.