

Long Term STOR Providers
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Dear Peter

Demand Side Balancing Reserve and Supplemental Balancing Reserve

The signatories to this letter are independent, small power plant developers. While they have a diverse range of business interests, they share an interest in long term STOR services and a desire to compete in the GB electricity market on a level playing field with the incumbents.

New Balancing Services

We believe that National Grid (NG) have devised their proposed new services without considering the impact on the wider market. The proposals would not be economic, compared to other options currently available, nor would they be transparent, but of greater concern is our belief that they are unduly discriminatory. While we acknowledge that there may be a tightening of the capacity margin in coming years, which as we approach winter 2015 could lead to concerns over security of supply, the case for NG's proposed new services has not been made.

The issue NG is attempting to address is the requirement to keep plant on-line at times of peak demand to make sure the lights stay on, but propose that this should not impact the wholesale market and be used only when in merit order, in the case of DSR, and as a last resort, for supplemental balancing reserve. In both cases we believe that the current reserve services can fulfil this role adequately. Unlike Grid's proposals, using an existing mechanism has some distinct advantages:

- Relatively easy and cheap to deliver, with existing systems, well developed contract terms, etc.;
- Does not interfere with the wholesale market as is despatched within gate closure period and held out of the market within its windows;
- Price is low and additional capacity is already being offered that could be taken up immediately; and
- Is economic and transparent, with the market understanding its use.

Demand Side Balancing Reserve

Everyone in the market is supportive of customers who wish to participate in the market being able to offer products and services that fit with their primary business operations. However, the feedback at NG's seminar seemed to be that the customers were already trying to wrestle with enough demand side scheme options (EMR, super red time bands, STOR, frequency response, etc.). There seems to be a view from NG that a new service will result in more customers participating, but it seems unlikely that this will be the case.

We would suggest that NG works with customers to enhance the schemes already in existence, rather than create new schemes. This should focus on discussions with parties who are not currently participating in the market and who may be willing to do so were the terms to be more attractive to them. This can be combined with the work DECC is doing on their pilot DSR scheme under the capacity mechanism proposal.

Supplemental Balancing Reserve

We have significant concerns with this new service and do not believe it should be introduced. It has numerous problems that would be costly to overcome, in terms of systems, codes, etc., especially for a scheme that will not be in place for very long. It also risks creating a "slippery slope" where the existence of the mechanism itself is likely to lead to further plant closures, as well as discouraging investment in new plant.

Were plant with SBR contracts to be warmed and despatched before gate closure and plant is then available in the balancing mechanism there will need to be some compensation given to the plant in the market. Without compensation, plant in the market will not earn the economic rent they expect, and the SBR plant is capping future prices, so those plants will look to close. This replacement pricing has significant system issues, the economics of which are unlikely to work given the proposed length of the scheme. The scheme runs a high risk of ending up with increasing volumes of capacity needing an SBR contract and could quickly become very costly.

For developers looking to build new plant, possibly with the capacity mechanism in mind, they are unlikely to want to bring forward investment until they understand the impact of SBR on the wholesale peak prices. This could further delay the very investment that DECC are hoping to encourage. This new plant will be more

efficient and have lower emissions than the plant the SBR is hoping to encourage to stay on line, so the cost of the service is likely to be higher.

If STOR were to be used instead of SBR it can be despatched only when other power in the market have been despatched or the plant available does not have the dynamics to meet the system needs. This will fit more with the last resort despatch NG suggest they are aiming for, unlike older plant requiring pre-gate closure warming. Given the type and cost of plant offering STOR services it is also likely to be the more economic solution.

Newer STOR plant is highly flexible, with lower emissions and often with extremely fast start times. Looking to the future the system will need more of this type of plant. DECC's capacity mechanism design, with a CONE (cost of new entry) based on an OCGT is also recognising the plant in STOR is exactly what the market will use as marginal plant 10-20 years into the future. A move in that direction today is simply a move in the direction of travel, not a market distortion.

STOR also maintains transparency as the market knows the plant is only despatched when BM plant cannot hit the dynamic requirements of the SO. Its operations are kept to a minimum and it does exactly what the service is designed for: making sure there is enough power on the system under a range of circumstances. We appreciate these circumstances may alter to accommodate a high demand, low wind day, but NG has already said that it was expecting to increase the volume of STOR to accommodate these sorts of issues in a market with higher wind and less conventional plant. Thus increasing STOR is a business as usual scenario and creates less market distortion and regulatory risk.

The process for buying STOR is also well established, with NG having experience in selecting plant based on a variety of factors, including the two price elements offered. SBR would be a new product, with three prices, and thus will take time and resources for NG to learn to purchase efficiently. We doubt efficient purchase can be achieved in a couple of years of experience.

Wider Issues

We have noted above that the services both seem to be unduly discriminatory; with embedded generation excluded from both services. NG has offered no reasonable explanation for excluding a part of the market that has historically provided large amount of reliable reserve through a variety of contracts. Issues around communications can be as easily overcome with an embedded generator as a customer. SBR appears equally applicable to older peaking plant, that may have existing systems, but could also be considering closure. These plants can easily provide the same MWhrs NG may require and possibly do so at a lower price. To rule them out of any new arrangements would not only be unduly discriminatory, but also detrimental to customers' interests.

If you or your colleagues wish to discuss any of the points raised further please do not hesitate to contact us.

Yours sincerely

pp

A handwritten signature in black ink that reads "Aislin Waters". The signature is written in a cursive style and is positioned on a light yellow rectangular background.

Alex Lambie, Chairman - Welsh Power Ltd

Mr M R Draper, Chief Executive Officer - Peak Gen Power Limited

Tim Emrich, Chief Operating Officer - UK Power Reserve Ltd

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