ukpowerreserve
SUPPORTING A RENEWABLE FUTURE

11/11/2013

Dear Mark,

Demand Side Balancing Reserve and Supplemental Balancing Reserve

UK Power Reserve Ltd is pleased to provide specific responses on the questions raised in the Demand Side Balancing Reserve and Supplemental Balancing Reserve in relation to National Grids Final Proposals Consultation. As an independent developer, operator and aggregator of flexible power generation assets, we have a strong interest in the questions raised in this document and it is in our interest to provide clear, concise and reasoned responses for consideration in future amendments and improvements in the procurement of reserve capacities.

About UK Power Reserve

UK Power Reserve is the leading independent developer and operator of flexible power generation in the UK. Founded by energy experts and investors in 2010, UK Power Reserve combines a specialist team and a portfolio of flexible energy generation assets. From site purchasing to operations and from plant design to grid connections, UK Power reserve brings a unique expertise to the UK energy market.

With its portfolio of flexible power plants, UK Power Reserve maintains security of supply and supports a renewable future as a provider of choice to the UK energy market. The pioneers of developing and acquiring flexible power generation, UK Power Reserve own and operate a rapidly expanding UK portfolio of generation capacity in addition to 3rd party STOR aggregation services.

Should you wish to further discuss any of the points in this response further, please do not hesitate to contact me.

Yours sincerely,

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UK Power Reserve Ltd
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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?

No, we feel the design of DSBR in relation to its proposed cost recovery and contractual interaction with other competitive Ancillary Services such as STOR creates distortions in the market and could potentially constitute State Aid support. Please see below for our detailed description of the identified issues;

Distortion in competitive markets

By enabling industry participants to enter into the DSBR service to receive upfront payments AND also contract and operate within the STOR commercial framework National Grid is creating additional routes to market within an already existing Ancillary Service such as STOR – this would serve to create additional competition within the STOR market and influence STOR market prices. This presents a market distortion issue on several levels;

1. National Grid proposes to recover costs of DSBR by passing through the costs within the Balancing Services Incentive Scheme (BSIS) –these costs are ultimately paid by the end consumer through electricity bills. By passing through the DSBR costs without an appropriate targeted/benchmarked incentive on National Grid – a conflict of interest arises - as there could be unintended consequences by creating additional competition for its other Balancing Services both through winter and summer periods. Additional competition within STOR is effectively being stimulated through subsidy - through pass through DSBR payments for DSBR providers that would otherwise not find the opportunity economic and therefore would not compete. This means existing STOR providers that cannot benefit from DSBR payments are not on a level playing field when tendering prices to National Grid.

2. Under DSBR National Grid proposes to pay an upfront payment to DSBR providers whilst STOR providers having secured contracts at competitive tender are effectively on pay as they earn contracts – this has the effect of creating an inequity on the economics when tendering across two ancillary services – creating inequalities between STOR providers that cannot benefit from DSBR payments.

3. State Aid support – reserves procured through Ancillary services by National Grid are done so as a mandatory requirement through their obligations under their System Operator (SO) Licence and are governed by licence condition C16 – the level of reserves procured are directly influenced by the wholesale energy markets. The amount of reserves required can be influenced by services delivered via interconnectors to the UK energy market. Introducing DSBR payments that are recovered on a cost pass through basis under BSIS to the end consumer could call into question State Aid support. This is an area that requires suitable legal review.

4. The introduction of DSBR will create additional security of supply options should the existing ancillary services become inadequate to service the short term operating reserve requirement to maintain a safe and reliable energy system. This in turn may have the effect of increasing National Grids risk appetite by effectively self-insuring reserve margins – therefore less reserve volumes could be procured through normal ancillary services such as STOR, Fast Reserve etc (targeted costs) as National Grid has more appetite for risk of running margins closer to the trigger point of using DSBR. As a result this may dampen National Grids appetite for procuring larger volumes of STOR ahead of real time to cater for this uncertainty.

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

No, we cannot support taking forward the DSBR product in its current design for the reasons mentioned in response to question 1. We could support this proposal if the following amendments were incorporated into the DSBR product;

1. Restrictions of DSBR providers from participating in any other National Grid Ancillary services for a period of 24 months from the delivery year. Our understanding is that any assets/initiatives in receipt of LCNF are not able to participate within STOR simultaneously. By placing restrictions similar to the restrictions in place on assets/initiatives in receipt of Low Carbon Network Funding (LCNF) the DSBR product would not distort short term price signals/economics of other Ancillary services (in our view current LCNF/ancillary service restrictions do not go far enough to prevent market distortions as highlighted in this response). A 24 month restriction seems reasonable and appropriate given the duration of STOR contracts that can be secured at tender up to a period of 24 months in duration.

2. DSBR payment should be on a pay as you earn basis rather than an upfront cost. Whilst we appreciate the reasoning of an upfront payment our view is that the DSBR payment should align with other Ancillary Service payments and be paid over the duration of the service period as opposed to being an upfront payment.

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 are of the view that TEC should be required to participate in SBR – we note National Grids views on this and as a result think that if TEC is not required then it should be a pre-requisite that only parties without TEC (or notified TEC reductions to zero for the contracting period) should be eligible to tender for the SBR product. By introducing a clear mandate around TEC National Grid ensures that;

- Prices are reflective of maintaining capacity to enter the market (regardless of need/utilisation).
- Capacity is procured from assets that would otherwise shut and not participate in the wholesale market in subsequent years.

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 agree procuring large volumes of extra STOR would cause distortion to the energy and balancing markets compared to SBR. We believe STOR could provide an appropriate platform to cater for the objective if National Grid split the STOR service into two distinct services –

- STOR – sites restricted to units with response times less than 30 minutes at 1MW or more.
- Supplemental STOR – sites with equal to or greater than 30 minute response times held in reserve for events triggered as per the SBR/DSBR proposals. This product could be open to all providers greater than 1MW (aligns to Balancing mechanism minimum requirement for despatch and monitoring purposes). This would not be too dissimilar to the Supplemental Standing Reserve process previously undertaken in 2005 and 2006 to secure additional reserves for the winter period.

We believe price comparisons would be inappropriate given the cost base differs between the SBR product and the STOR product. To enable potential SBR providers to tender without the need for Transmission Entry Capacity (TEC) the SBR provider has a reduced cost base and therefore tender prices should be more competitive than for providers tendering into a more active ancillary service such as STOR, as with STOR TEC is required.

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 recognise the issues National Grid as System Operator face with maintaining short term security of supply against a backdrop of diminishing capacity margins. Our preference would be no intervention through the proposed additional ancillary services such as DSBR and SBR, however, if presented with the choice on offer we feel the SBR product is a better option to implement than the DSBR product (please also see our response to Q4). Our reasoning is that the SBR product will provide the safety net required using existing providers that can be delivered in volume and at least cost using existing systems already in place. This would represent the best value option for the end consumer and deliver the objective of insuring capacity margins over the short term whilst longer term initiatives are progressed. We also believe there are already sufficient Demand Side options under development within the industry that are better aligned to encouraging and promoting Demand Side reserves (LCNF, STOR & Capacity Market DSR Trial) .

We would also emphasise the importance of the EBSCR regarding the amendments to imbalance and cash out and how vital timely implementation of this proposal is in the context of incentivising and securing additional capacity to support a safe and reliable energy system.

Costs & Funding Questions

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

For both DSBR and SBR we believe a targeted/benchmarked incentive on the costs associated is required. The service costs should reflect value of money for the end consumer and be comparative when compared to the value of other ancillary services. Although we appreciate the reasoning for not including these costs under the targeted BSIS model we have concerns that the values referenced within

the proposals are out of date – especially given the recent STOR Tender Round 21 Market Report publication (08/11/13) that reflects average availability payments £1.84/MW/hr. for the 2014 summer which reduces to £1.27/MW/hr. for the 2014 winter period. These most recent price signals are far lower than the benchmarks referenced in the consultation proposal and demonstrate how difficult it is for National Grid to forecast prices and limit distortions when considering procurement of additional ancillary services.

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

We feel it would be appropriate that a discounted price mechanism could be designed to provide some certainty on prices/volumes and incorporated into BSIS under a targeted model to provide adequate/accurate benchmark costs to existing ancillary services. This would provide additional comfort that costs are reflective of the value of the service being offered and do not create further price signal distortions.

Q8. Do you agree with the proposed approach to the recovery incremental internal costs we would incur if we were to procure these additional balancing tools?

The proposed approach of cost recovery is appropriate.