

SO Incentive Scheme Initial Proposals– Association Response

20 January 2005

Introduction The Association welcomes the opportunity to respond to the Ofgem consultation on the SO Incentive scheme – Initial proposals. The Association of Electricity Producers (AEP) is the UK trade association representing electricity generators. It has some 100 members ranging from small firms to large, well-known PLCs. Between them they embrace nearly every generating technology used in the UK. Many member companies have interests in the production and development of renewable energy where the government has set ambitious targets for development over the next decades.

Detailed Comments:

1. Scope and Duration of the Scheme The Association accepts that, for a one-year extension of the scheme, it is appropriate not to disturb the scope. We support a one-year extension as a reasonable incremental strategy that gives time to develop a longer term scheme.
2. Transmission Losses We welcome the further explanation on the contribution of transmission losses to the SO Incentive Scheme. We have some remaining concerns about the way in which transmission losses are factored into the scheme, but suggest that these are explored in the coming year as we move towards a longer term approach to incentivising the GB SO.
3. Sliding Scale Scheme The Association accepts the basic sliding scale approach.
  - a. Sharing Factors: For this scheme, we continue to believe that NGC's sharing factors have been and remain overly generous considering the maturity of the scheme and reduced scope NGC has for any innovation.
  - b. Symmetry of Sharing: The Association would not support asymmetric sharing factors, unless there is a demonstrable asymmetry of risk. The tiny skew on NGC's overall forecast of IBC costs (page 147) is not sufficient to warrant asymmetric sharing factors.

In the event that there is truly an unforeseeable event that skews the risk, NGC can still have resort to the IAE process. Following the recent Ofgem consultation, this process should be more amenable to scrutiny by the rest of the industry than was previously possible.

- c. Deadband: We accept Ofgem's conclusions that NGC should manage costs across the range and that therefore a deadband is not appropriate.
2. Delay to BETTA Go-Live: We do not anticipate a delay to Go-Live. In the unlikely event that it is delayed, pro-rated extension of the current E&W scheme is one way of dealing with the issue pragmatically. In general, we are relaxed about the detail of how a short delay would be dealt with.
4. Value of Schemes Ofgem propose to offer NGC the choice of three schemes. All of these options represent a significant discount compared to NGC's forecast. Ofgem's analysis of outturn versus forecast for NGC has clearly

shown NGC's very conservative approach to forecasting. However, we would query the proposal to offer NGC three schemes from which to choose.

5. Future of the Scheme: The next two years can be profitably spent in reviewing the current components of the scheme with a view to replacing them by more market based arrangements wherever possible and trialling those arrangements in the second year. In this regard we note that this consultation document offers fuller explanation of some of the components of the scheme and increased transparency of both Ofgem's and NGC's approach to quantifying these components and how they might change. We welcome this increased transparency and look forward to its further extension. In order to build on the previous schemes we would suggest that a mid-year analysis of performance against the scheme is performed. This will allow the lessons from BETTA to start to be incorporated into future schemes as soon as possible. The Association and its members look forward to full involvement in such a review. Where there is a market-based mechanism, NGT will not need an incentive to make the most economically rational choice, because the market will deliver the best available economic answer to the question of balancing the system. We recognise that some components of the current scheme, such as management of constraints will probably have to remain in the province of an administered scheme; the second-best answer after more market-based arrangements. Nevertheless, we look forward to Ofgem's proposals for longer-term more market-based arrangements.
6. Network Reliability Incentive Scheme: The Association does not think the proposed scheme is good value for customers' money. Notwithstanding this, we seek assurance that Ofgem has the means to police any overlap and therefore avoid double incentivising between the schemes.