

# 2007/8 Electricity Balancing Services Incentive Scheme

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# Agenda

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- ◆ Overview
- ◆ Incentive outline
- ◆ Forecast overview
- ◆ BSUoS
- ◆ Other scheme proposals

# Electricity Incentive scheme process

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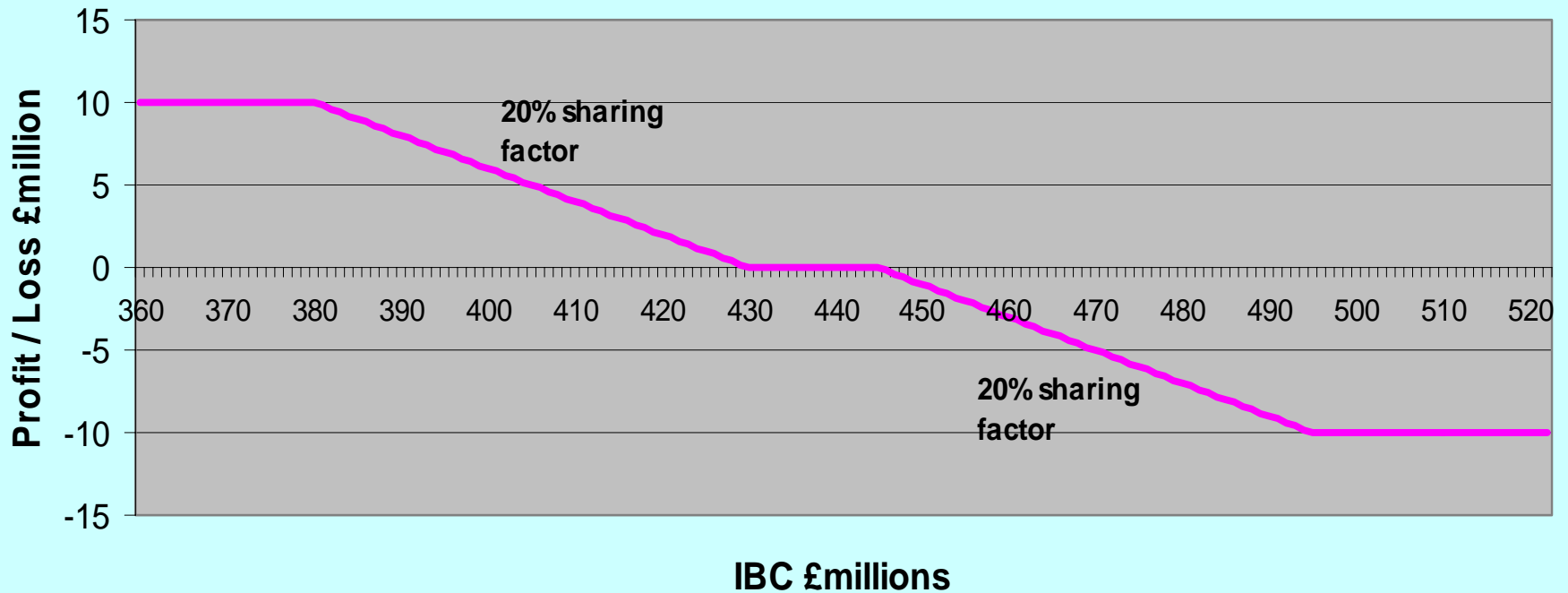
- ◆ Invitation to submit views by Ofgem on 5 July 2006
- ◆ Preliminary views consultation on 2 October 2006
- ◆ Initial proposals consultation 5 December 2006
- ◆ Seminar on Costs of Electricity System Operation - 10 January 2007
- ◆ Final proposals and statutory license consultation on 27 February 2007
- ◆ Incentive arrangements start 1 April 2007 for one year

# 2007/8 Overview

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- ◆ National Grid has accepted the proposals set out in the latest consultation
- ◆ Similar format for scheme as previous years
- ◆ Scheme runs for one year
- ◆ Scheme presents a very challenging target

# Proposed scheme



# Ofgem Rational

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- ◆ Ofgem estimated outturn at £430Million
- ◆ Rational for difference to National Grid's forecast was:
  - ◆ decreasing wholesale price trend
    - ◆ pressure on decreasing constraint costs
  - ◆ industry consultation responses cited:
    - ◆ frequency response costs were stabilising
    - ◆ use of contractual arrangements to reduce constraint costs
    - ◆ perception that National Grid has a history of over-forecasting

# National Grid's 2007/8 Forecasts

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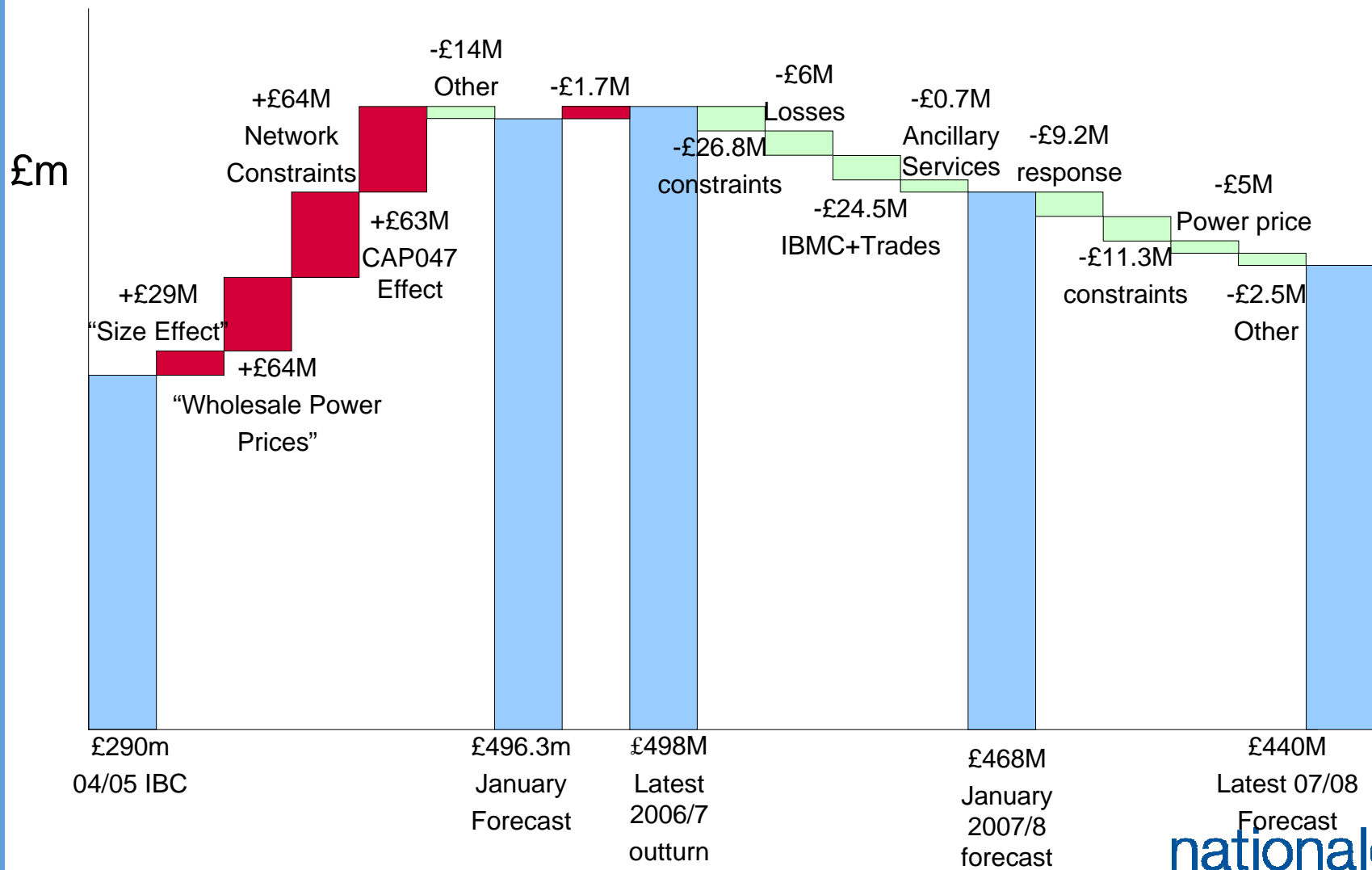
- ◆ Initial forecast was £458M
- ◆ January revised forecast was £468M
  - ◆ Increased from original due to estimated costs of frequency response, constraints and reserve

# Forecast changes

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- ◆ Latest forecast - £440M
  - ◆ Power price changes £5m
    - ◆ Power price reduction of £1.75 MWh
  - ◆ Revised constraint £11.3m
    - ◆ Updated outage plan – still changing
    - ◆ Assume we do not contract for certain strategic generation in Scotland
  - ◆ Updated frequency response forecasts £9.2m
    - ◆ Submitted prices under CAP047 may not increase as first thought decreasing response price based on industry feedback given to Ofgem;
    - ◆ We intend to increase our procurement efficiency of response services
  - ◆ Other forecast changes £2.5m

# Main Cost Driver Impacts Illustrated



# 2007/8 Cost Breakdown

	2005/6	2006/7	2007/8
Ancillary Services	228.1	309	308.3
Constraints	79.7	109	82.2
Transmission Losses	-5.5	6.0	0.0
IBMC+Trades	125.2	74	49.5
Total	427.5	498	440

# 2007/8 ancillary services cost breakdown

	2005/6	2006/7	2007/8
Reactive	54.7	54.2	41
Response	65.4	117.9	116.5
Reserve	92.5	117.6	130.0
Other	15.5	19.3	20.7
Total	228.1	309.0	308.3

# Uncertainties and risks

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- ◆ Margin / reserve >£10M
  - ◆ Weather dependant
  - ◆ A Change in market length can cause considerable spikes in costs
- ◆ Power Price >£10M
  - ◆ Power prices have fallen significantly
  - ◆ Future trends unknown
- ◆ Constraints >£10M
  - ◆ Dependant on bidding strategy
- ◆ Frequency response costs >£10M
  - ◆ Prices have risen three fold since CAP047 introduction
  - ◆ Increasing cost trend
- ◆ Code modifications
  - ◆ Unknown changes and potential costs

# Initiatives to meet target and manage risks

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- ◆ Constraints
  - ◆ Assessing applicability of previous risk mitigation e.g. contracts
  - ◆ Considering new strategies
- ◆ Frequency response costs
  - ◆ Continued focus on process and procurement improvements
  - ◆ Continually seeking out new service providers
  - ◆ Considering changes to procurement mechanism(s)
  - ◆ Code modifications
- ◆ Margin / reserve
  - ◆ New BM Start-up introduced in November 06
    - ◆ Some benefits being realised
  - ◆ Standing reserve – STOR
    - ◆ Initiatives to attract more providers

# What does this mean for BSUoS?

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- ◆ BSUoS is made up of a number of components
  - ◆ SO external costs - £500 - £545 Million
    - ◆ Net energy imbalance adjustment £60M - £105M
  - ◆ SO internal costs - £108M
- ◆ BSUoS projected to be around £608 - £653 Million
  - ◆ Many caveats associated with the forecast
  - ◆ Using estimated 2006/7 volumes, provides £0.94/MWh to £1.005/MWh BSUoS charge

# Additional Ofgem proposal detail

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- ◆ Proposal outlines the areas where Ofgem believes National Grid can develop additional services / providers
- ◆ Provides clarification on provisions to report anti-competitive behaviour
- ◆ Clarification on what constitutes an Income Adjusting Events

# Additional Ofgem proposal detail (cont)

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- ◆ If any party believe someone is abusing their market power, Ofgem would expect them to make a complaint under the Competition Act
  - ◆ Considering what information may be required
  - ◆ Looking internally at implications and instances where this may be applied
- ◆ No specific provisions outlined for an IAE
- ◆ Events where IAE's can be raised are the same as previous years:
  - ◆ Force majeure
  - ◆ Fundamental changes in the wholesale energy markets
    - ◆ E.g. significant unexpected change in power price

# Summary

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- ◆ National Grid has agreed a one year incentive deal
- ◆ Challenging targets
- ◆ National Grid's current forecast is in the incentive scheme deadband i.e. no projected profit or loss
- ◆ Number of risks and opportunities to deviate from target
- ◆ Significant number of ongoing initiatives being progressed to realise opportunities and mitigate risks