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Dear Lord Mogg

National Grid (www.nationalgrid.com) is one of Europe's largest energy transmission companies. In addition to our activities as the UK's principal Electricity and Gas Transmission System Operator, we are a major gas distributor in England and a leading energy utility in the United States.

National Grid welcomes the publication of this consultation by ACER covering European energy policy regulation through to 2025. This clear communication by European Regulators of their views on the current direction of travel for the Energy Industry is, as well as their anticipated future possible future regulatory actions, very much welcomed. National Grid would like to comment on some of the broad topics covered within the consultation, and where appropriate, provide a view on the relative priority of the proposed areas of future work. To summarise the key elements:

- The finalisation of the European Network Codes (ENCs) should remain a high priority. The European regulatory framework should support and facilitate implementation of the ENCs and allow time to assess their results before further changes to the market framework are proposed.
- Closer coordination between the gas and electricity systems should be investigated with the aim of allowing greater system flexibility and more efficient and innovative solutions to current challenges.
- ACER has an opportunity to add significant value by utilising its current NRA coordination role on issues relating to differences of opinion over cross-border investment and cost allocation.
- The industry should consider options for developing more effective ways of amending and modifying ENCs. Industry could be permitted to propose ENC modification changes.

Integrated Markets

National Grid believes that the finalisation of the European Network Codes (ENCs) is of the very highest priority as they are the fundamental foundation for achieving the benefits from the Target Model. They will permit and foster greater cross border interconnection, and therefore trade. This will ultimately lead to a whole raft of benefits to end consumers, not least reducing the costs to which they

are exposed. The ENCs application and implementation stages, following Comitology, will take substantial time and effort from each Member State and therefore it is key that any blockers preventing the completion of Comitology are overcome. Many of the proposed future benefits discussed in this consultation, for example enhance inter-TSO cooperation, can only be initiated once many of the elements of the ENCs are finalised. The speeding up of the finalisation of the Network Codes has been discussed both in the recent Commission Communication on a European Energy Security Strategy and at several recent Council meetings.

National Grid agrees with the impacts identified relating to non-programmable renewable energy, however one element that may have been overlooked is how the unpredictability of such generation will not only impact electricity networks but also the gas transmission and distribution networks. We agree that greater TSO to TSO and TSO to DSO coordination is an essential element to mitigate such effects and therefore reinforce the principle that sufficient physical interconnection should be in place to facilitate such coordination.

Electricity: National Grid supports the proposed efforts to develop cross-border European balancing markets, such as the balancing pilot projects and are actively engaged in and contributing to the process of developing balancing options, which will ultimately maximise social welfare. However, where countries have chosen to organise their balancing markets in different ways, methodologies and options need to be developed which overcome these differences without requiring wholesale change in market design right across Europe. National Grid also supports the view that greater flexibility and liquidity in cross border balancing is required, and advocates further development of European balancing options in all timescales, addressing in particular the creation of common balancing regimes on those borders where significant differences in market design exist.

We broadly agree with the principles and actions expressed around intervention in electricity markets and generation adequacy and believe that the anticipated design of the proposed mechanisms in the UK is complementary to these principles.

Gas: We agree that greater penetration of renewables in electricity generation will create the need for greater levels of flexibility within the gas network in order to support the growing dependence on CCGT gas fired generation to support the electricity network at times of variable renewables output. Clearly gas back-up generation has the potential to contribute more to the sustainability agenda due to the lower carbon content of natural gas than other fossil fuels. However, the need to be appropriately remunerated for this flexibility extends beyond the needs of the gas fired plant. The provision of the necessary gas network flexibility for the limited number of hours each day requires the gas TSO to reserve and maintain this flexibility. As such, the assets provided, maintained and operated in order to provide such support to the CCGTs (and, in turn, the electricity network) also need to be funded. National Grid feels it would be inappropriate for gas consumers to fund such provision of flexibility and therefore the costs of its provision should be recovered from the electricity market via charges either directly to the gas fired generator or via other more generalist charging.

It is also clear that the timings of the flexibility requirement within the electricity network (a limited number of hours within each day) are likely to be inconsistent with the daily balancing timeframe within the gas market and the current EU Gas Balancing Network Code. As such it is possible that the actions (needed for short term access to system flexibility) of the Gas-fired plant could result in a shortfall or surplus of gas within the gas network as the plant responds to the immediate need for flexibility within the electricity network whereas the associated gas shipper is incentivised to take action to rebalance its gas portfolio by the end of the gas day thus leading to a mis-match of timeframes. This may therefore lead to greater residual system balancing actions by the relevant gas TSO as it seeks to maintain system integrity during the above mis-matched timeframes. Given that the gas TSO is neutral to such residual balancing actions, National Grid considers it will again be

important, where possible, to seek to ensure that the net costs of such residual balancing actions are efficiently targeted towards the energy consumers who receive the benefits of such actions i.e. electricity consumers. Failure to achieve such cost targeting would potentially result in a subset of consumers (gas) inefficiently subsidising a broader set of consumers (electricity).

Energy Consumers

The focus on increases to end consumer bills has been correctly identified as an ongoing priority. The building of cross-border interconnectors and a truly-interconnected European market offers significant opportunities in this respect. In addition, National Grid believe that increases to end consumer bills can be mitigated by ensuring that innovative products and services are developed which provide cost reflective signals to consumers, so that the benefits from changes in energy usage behaviour can be positively reflected back, such as “time of use” pricing. This will be essential to manage the volatility of new electricity generation sources and support efficient system utilisation of energy networks, avoiding otherwise necessary system reinforcement and ultimately reducing costs to end consumers overall.

A workable commercial and regulatory framework for demand flexibility products is essential. It will be important, however, for such a framework to be flexible enough to enable innovative products to be developed for the market which will offer genuine value to system operators.

The Future Role of DSOs

National Grid is keen to embrace the concepts of active DSOs and how they can develop into an overall DSO framework. There are a range of issues that we believe require addressing before the full benefit from DSOs can be realised. Firstly, to date, there has been discussion on a number of possible models and roles that could potentially exist for the future DSO. This list needs to be finalised so the complete list of ‘types’ of DSOs can be confirmed. In addition, an understanding must be developed for how other industry stakeholders integrate and interface with the future DSO role.

Gas Distribution will play a pivotal role in providing heat and generation over the next decade, enabling opportunities for sustainable fuels to connect and maximising the efficient use of the existing gas network. National Grid agrees that, as production and utilisation of gas migrates towards a more local focus (bio-gas/shale gas delivery directly into the distribution networks and/or growth of gas use in the transport sector), it will be important to recognise and fund the increased roles and responsibilities of the DSOs in facilitating the new requirements, maintaining these energy delivery routes and security of supplies. As alternative technologies progress, the Gas Distribution network can be utilised to avoid investment in the Electricity Distribution systems, thus supporting demand side response via smart metering. Gas networks are already able to successfully respond to customer variability, the next steps are evolutions of this principle and require little change to the network. National Grid also agrees that it is equally important that the role of the DSOs should be appropriately minimised in order to maximise the competitive market for services such as those detailed in the consultation document.

Infrastructure Investment

National Grid is in general agreement with the statements made concerning infrastructure investment, and in particular would like to highlight the point made that infrastructure investments that span national borders are of an order of magnitude more complex than those within a single Member State and therefore under a single regulatory framework. National Grid is currently actively engaged in several initiatives that are reviewing cost allocation and system enhancement models for

interconnecting infrastructures which should complement future work when considering how to facilitate interconnector infrastructure investment. National Grid believes that stronger cooperation between NRAs on issues relating to cross-border cost allocation would be helpful when it comes to necessary investment and consider that this is a key area where the current clear coordinating role of ACER can add value.

Investment challenges remain a particular concern for gas, partly due to current regulatory initiatives creating incentives towards short-term capacity bookings. The absence of longer term capacity bookings will give rise to increased revenue volatility for TSOs. National Grid welcomes the goal to ensure the minimisation of stranded assets but we need to ensure consistency across European energy objectives. There is a clear need for investment in certain areas in order to further the EU internal gas market but uncertainty over future gas demand is hampering this objective.

Governance

We support increased cooperation between electricity and gas TSOs and National Grid is an active member of both ENTSO-E and ENTSO-G. We believe that there is scope to consider the merits of closer coordination between gas and electricity system operators to ensure the integrity of the respective systems and maximise the ability of gas fired generation to provide back-up for renewables generation. In this respect, we believe it could be beneficial to investigate the current regulatory separation between the near real-time interaction between electricity and gas TSOs, where closer interaction and coordination may lead to greater efficiency and flexibility. That withstanding, we recognise that coordination between gas and electricity real time operations is more problematic as there are risks of inappropriate cost transfer.

National Grid believes that the roles of the ENTSO-E and ENTSO-G are well defined in the Third Energy package and that the organisations are working effectively and we therefore do not foresee a need for an expanded role for the ENTSO's or for ACER. National Grid believes that the level of harmonisation achieved thus far in Europe has been helpful but further enforced centralisation of national TSO tasks risks giving rise to inefficiencies and an erosion of local/ national flexibility that can benefit consumers. The focus should rather be on the implementation of existing measures such as network codes.

National Grid believes that there is scope to consider more effective ways of amending and modifying European network codes, although any such process should include a strong element of industry and stakeholder involvement. National Grid believes that a process whereby industry could propose modification changes, (as well as NRAs), would be an extremely effective way of developing successful market designs that would eventually achieve regulatory approval. In GB, the successful gas and electricity markets have been achieved through the industry and Ofgem agreeing key principles and then constant evolution of the detailed rules, sometimes driven by ourselves, sometimes by Ofgem and sometimes by industry participants – always, however, with a strong ethos of inclusive and transparent development and decision making. National Grid also believes that further consideration may be required from European Regulators on how the Network Codes are nationally implemented. For example, the precise basis on which their benefit is assessed, for example, individual Member State vs Community wide benefit or consumer vs societal benefit.

National Grid has been an active member of the Regional Security Coordination Centre, Coreso, since 2009. National Grid sees Regional Security Coordination Centres as a positive development facilitating another layer of coordinated operational system analysis. However, it is believed that at this point in time a formal regulatory framework may hinder their development and evolution and is probably not warranted as a result of the inherently regulated nature of their TSO constituent

members. In addition, the operational European Network Codes set out the foundations for common practices and coordination in pan-European operational security and therefore there may be real value in letting these bed-in before further arrangements are developed.

Yours sincerely

Paul Whittaker
Director, UK Regulation



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