

**DECC Consultation - Response to Synergies and Conflicts of Interest arising from the GB System
Operator delivering Electricity Market Reform**

Submission by GDF SUEZ Energy International

(I) About GDF Suez Energy International

GDF SUEZ Energy International (formerly known as International Power) is responsible for GDF SUEZ's energy activities in 30 countries across six regions worldwide (Latin America, North America, the Middle East, Turkey & Africa, UK-Europe, Asia, and Australia). Together with power generation, we are also active in closely linked businesses including downstream LNG, gas distribution, desalination and retail. GDF SUEZ Energy International has a strong presence in its markets with 77 GW gross capacity in operation and a significant programme of 10 GW gross capacity of projects under construction as at 30 June 2012.

The UK-Europe region (GDF SUEZ Energy UK-Europe) has 13.9 GW gross capacity in operation, which includes over 9.2 GW of plant in the UK market made up of a mixed portfolio of assets – coal, gas, CHP, wind, a large open cycle diesel plant, and the UK's foremost pumped storage facility. Several of these assets are owned and operated in partnership with Mitsui & Co. Ltd. The generation assets represent just under 9% of the UK's installed capacity, making GDF SUEZ Energy UK-Europe the country's largest independent power producer. The company also has a retail supply business and a significant gas supply business in the UK, both serving the Industrial and Commercial sector.

(II) Summary key points

- DECC has chosen National Grid as the EMR delivery body due to the perceived potential for strong synergies with the current role of the System Operator (SO). GDF SUEZ believes greater benefit would arise if the EMR delivery body has the best possible information.
- If information that is provided for the EMR delivery body is utilised for another purpose within NG (e.g. within the SO or TO environment) this will undermine the basis of information provision and is likely to result in lower quality information being provided than would otherwise be the case and lead to inefficient delivery of electricity market reforms.
- As a minimum, GDF SUEZ believes that initially there should be legal separation of the EMR delivery role through a ring fenced entity required to act independently of the other National Grid businesses. The ELEXON arrangement could offer an appropriate model.
- In the longer term, if it becomes apparent that synergistic opportunities are being missed, then consideration should be given to combining parts of the function with the EMR role where there is no possibility that confidential information will be shared. Until that time, the default position should be full separation.

(III) General comments on the consultation

1. This response focuses on generic messages rather than answering the specific questions posed as the latter focus on the scope for synergies, degrees of materiality and mitigation measures. Since GDF SUEZ firmly believes in the necessity of a legally separate EMR Delivery function, this response does not address the specific questions in the consultation.
2. GDF SUEZ agrees that there is the potential for conflicts in the competitive areas of National Grid's businesses and that it is appropriate for the EMR function to be kept separate from these competitive areas. We have therefore focussed this response on the potential for conflicts and synergies in the TO and SO roles.

(IV) Potential for synergies

3. DECC has chosen National Grid as the EMR delivery body due to the perceived potential for strong synergies with the current role of the System Operator (SO). The consultation notes that *'the cost of operating the system (balancing the system and managing constraints) was £886m in 2011/12'* and that *'the main benefit with the SO arises from access to information that would allow it to lower its balancing costs'*. DECC concludes that since National Grid made £9m of operating profit in its SO role then the potential for conflict is quite small.
4. GDF SUEZ believes that DECC is focussing its conclusion on whether the SO could gain from this information. DECC should also consider the much wider and much larger benefit of the EMR delivery function having good information to allow the objectives of EMR to be achieved at least cost to consumers.
5. Government estimates that some £110bn will need to be spent over the next decade¹ to replace our ageing energy infrastructure with a more diverse and low-carbon energy mix, while minimising consumer bills.
6. Having good quality information will help to minimise the very substantial cost of achieving the desired reforms. The benefit of having confidence in the information provided would seem to far outweigh what would seem to be a relatively much smaller reduction in balancing services costs. There have not for example been many responses to the National Grid's call for evidence on CfD FiT strike prices, perhaps due to concerns as to how this information could be used.
7. GDF SUEZ believes that the synergies may in any case have been overstated. Under the proposals for both the CfD and the capacity mechanism, planning consent and a grid connection will be prerequisites before low carbon generation can apply for a CfD and new entry fossil generation for a capacity contract. This information will already be public; National Grid has to make grid connection offers and planning applications can be tracked. The SO/TO parts of National Grid will therefore already have sight of this information. Placing the SO and EMR functions together would not seem to create any additional synergy with respect to system planning decisions.

¹ http://www.decc.gov.uk/en/content/cms/meeting_energy/markets/electricity/electricity.aspx

(V) Potential for conflicts

8. As with the previous consultation on conflicts of interest, it is difficult for respondents to be precise about where conflicts might occur when the details of the CfD and the capacity mechanism have not been fully defined. Until there is clarity it would be sensible to create a clear separation of the EMR role from the rest of National Grid. To give a few examples:
- In determining the reliability standard and hence the amount of capacity to procure under the capacity mechanism, the Minister will be dependent on advice given by National Grid. Questions could be raised as to whether the advice National Grid gives benefits its regulatory asset base.
 - Under the capacity mechanism, it is not yet clear whether existing plant will have to justify non zero bids. If they do, then this pricing information should be treated as confidential and it would not be appropriate for the SO function to have sight of this information.
 - Despite itself being a private company with a shareholder base to serve, the SO will be awarding contracts to other private companies. Even if National Grid can only award these contracts against defined criteria, a separation would avoid any perception that National Grid is serving its own purposes.
 - Even if there is a strict mechanistic model for awarding contracts, at a later date, National Grid will have to make rationing decisions when the Levy Control Framework starts to bite. It is not yet clear how projects will be rationed and how information provided by CfD applicants might be used, not only in the rationing process, but also how the information could propagate through other parts of National Grid.
9. If the main rationale for internalising the EMR delivery role within National Grid is the perceived synergies that can be achieved through information sharing with the SO then GDF SUEZ does not think the case has been sufficiently well made. If this synergy is absent, there seems little sense in retaining the EMR delivery role with the current structure of National Grid.

(VI) Views of the Institutional Frameworks Expert Group

10. The concerns highlighted above are not new. GDF SUEZ notes DECC's minutes of the Institutional Frameworks expert group at their meeting on 21st September 2012:
- *There was a strong preference within the group for the EMR functions to be ring fenced and managed under a separate licence.*
 - *There were a number of justifications for this approach:*
 - *It would be necessary to provide the market with the level of confidence required given the highly sensitive nature of the information provided to National Grid;*
 - *Separation sends a clear signal and demonstrable commitment to manage the potential conflicts;*

- *Separation creates a distinct atmosphere and culture within the EMR team;*
- *NG has already taken similar measures in relation to ELEXON;*
- *Separation deals with conflicts early – preventing or reducing the potential for conflicts further down the line; and*
- *Even if there were no conflicts of interest, it would be logical to have a new EMR body with a new licence as EMR is a new activity in the market.*

11. GDF SUEZ Energy UK-Europe strongly agrees with these justifications and in particular the preference for the EMR functions to be ring fenced and managed under a separate licence.

(VII) Extent of separation of EMR Delivery Body and System Operator

12. As a minimum, GDF SUEZ believes that a legally separate EMR function should be created with the directors of the EMR ring fenced entity required to act independently of other National Grid businesses. This could take the form of an ELEXON type organisation². Given this position, we have not addressed the specific questions in the consultation as they relate to the potential for synergies and conflicts and degrees of mitigation. The above position makes clear the extent of mitigation that GDF SUEZ would like to see as a minimum.
13. If in future, it can be established that synergies are being missed through this separation and that those synergies do not require the sharing of confidential information, then it would be sensible to allow those parts of National Grid and the EMR function to be combined. Until that time, the default position should be full separation. In the unlikely event that National Grid is unable to fulfil its EMR role, it would also be a less difficult challenge for a new entity to take on.

² Whilst ELEXON is a wholly owned subsidiary of National Grid Electricity Transmission (NGET), NGET does not have a place on ELEXON's Board and has no financial or other obligations or management control over ELEXON.

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