

# Information Note

**Friday 4 May 2012**

## **OFGEM TAKES NEXT STEP TOWARDS NEW TRANSMISSION CHARGING STRUCTURE**

Ofgem has today taken the next step toward a new approach to transmission charging. It is requiring industry to develop changes to the current charging approach which will better reflect the costs placed on the system by all forms of generation, particularly renewable generators, which operate intermittently. The aim of the changes is to facilitate Britain's transition to a low carbon energy sector at the lowest cost to consumers.

The existing methodology, known as Investment Cost Related Pricing (ICRP), charges generators more the further they are located from demand. The new approach will retain this locational element but update it to take into account the type of generator and how much it uses the network to transmit power. In doing this, Ofgem considers that an improved form of ICRP would better reflect the costs placed on the high voltage system by all forms of generation, including new kinds of generators such as wind farms.

In line with normal procedures, **Ofgem is now requiring industry to further develop an improved form of ICRP.** Once this work is complete Ofgem will consider the findings and make a decision on the modification.

Overall transmission charges make up four per cent of an average household bill and the cost to consumers of any potential change was a key consideration in Ofgem's review. Ofgem would expect any proposal to ensure that any changes to transmission costs would have a minimal impact on consumer bills.

In addition to improved ICRP and retaining the current approach, Ofgem also consulted on socialisation which would charge generators the same regardless of location. Ofgem sees this as a much less desirable approach to transmission charging as initial modelling suggests it would result in increased overall costs of £7bn for consumers, exacerbating existing patterns of fuel poverty with no proven overall benefit to consumers.

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### **Notes to editors**

#### **[Project TransmiT - Electricity transmission charging arrangements Significant Code Review conclusions](#)**

##### **1. Scottish Islands**

While Ofgem has directed industry to further develop how an improved form of ICRP applies to the Scottish islands, the approach will retain the locational element of transmission charging. In the case of Orkney, Shetland and the Western Isles, which by their nature are located very far from demand, there are currently no high-voltage connections from them to the mainland. Therefore the infrastructure costs required by them to transmit power to the mainland are very high and this would be reflected in the transmission charges for these generators.

However, a key aim of Ofgem's review of transmission charging has been to facilitate a move to a low carbon economy. An improved form of ICRP would more accurately reflect the costs that intermittent generators, such as wind farms which only generate when the wind is blowing. Although the effect of this will vary across the country, for the Scottish islands, following the installation of the high-voltage connections to the mainland, they could stand to benefit by close to a 50% reduction in charges for use of the main network compared to the current situation.

## **2. What are transmission charges?**

Transmission charges are paid by generators and suppliers for using the high voltage electricity network across Great Britain. Generators pay charges to flow power across the network while suppliers pay charges to take power from the network and transport it to their customers (i.e. businesses and homes). They account for four per cent of a household power bill. Generators face higher charges to transmit power the further they are located away from areas of high electricity demand as it costs more to transport their energy to consumers. Generators in the south of England pay lower charges, and in some cases receive payments. This is because they help National Grid avoid investment in reinforcing the high voltage grid.

## **3. How are transmission charges set?**

Transmission charges for generators and suppliers are set by National Grid using a formula approved by Ofgem. The charges pay for running the high voltage networks. Charges are paid to National Grid in its role as the System Operator for Great Britain and National Grid recovers these costs from all users of the grid, both generators and electricity suppliers. This means generators pay charges to transmit power while businesses and homes pay for electricity to be transported to them as part of their bills. Location based charges have been in place in England & Wales since 1990 and were introduced GB wide in 2005 to better reflect the costs National Grid faces for running the high voltage grid.

**4.** Ofgem is the Office of the Gas and Electricity Markets, which supports the Gas and Electricity Markets Authority, the regulator of the gas and electricity industries in Great Britain. The Authority's powers and duties are largely provided for in statute, principally the Gas Act 1986, the Electricity Act 1989, the Utilities Act 2000, the Competition Act 1998, the Enterprise Act 2002, the Energy Act 2004 as well as arising from directly effective European Community legislation.

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