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Dear Andrew

Targeted Charging Review Response: Ecotricity

Ecotricity has an interest in this consultation as an Ofgem licensed renewable energy supplier which also develops renewable energy generation to supply to our customers over the electricity network and through private wire installations. We therefore believe we will be significantly affected by changes considered in this consultation in several different capacities.

Executive Summary: Ecotricity's position as regards is that, for the reasons set out below, Ofgem should delay this TCR until the Significant Code Review for Access and Forward Looking Charges (SCR) has been completed by Autumn 2020.

While we agree with the TCR principles it's a concern for us that the consultation does not include wider legally binding Government and industry objectives of carbon reduction and energy efficiency. The changes proposed may reduce carbon emissions from distributed diesel generators but will also catch forms of clean energy generation. We would ask Ofgem to reconsider including a carbon reduction, energy efficiency or broader industry strategy principle to ensure this TCR aligns with overall policy and to minimise unintended consequences that must be addressed further down the line.

As has no doubt been stated by other parties the sheer amount and rate of reform occurring in the industry at this time is of concern. Whilst we realise Ofgem is aware of this and is trying to balance the need to change with the need for stability, we would like to stress just how this rate of change is:

1. Investor confidence is damaged and risks delaying and raising the cost of new developments. A perfect storm of regulatory change, Capacity Market suspension and needless to say Brexit makes this a hugely uncertain time to invest in our energy network.
2. Smaller players in the market often struggle to dedicate sufficient resource to participate in all of the industry changes to ensure their voice is heard. The volume of change at present is overwhelming and means there simply isn't time for smaller players to engage fully with every consultation that they should. Trying to provide the necessary evidence to back up their arguments is also often beyond the means of their limited resources.
3. The impacts of different changes are likely to overlap and affect each other making impact assessments of one change meaningless until the outcome of another is known. Having different consultations and changes working within their own narrow scope can result in inconsistent outcomes. It is this that concerns us most about this TCR.

The Significant Code Review for Access and Forward Looking Charges is currently underway and not due to consult on a decision until Spring 2020 and make a final decision in Autumn 2020. As we understand it, the residual charges covered by this TCR are a means for 'topping up' Network companies' income to their entitled levels. Therefore, residual charges are determined by the price controls and the size of Forward Looking Charges. Currently, residual charges make up around 80%

of transmission charges and 50% of distribution charges[1] which indicates these are not being used as a 'top-up' as intended but in fact represent the bulk of network charging.

In our view the SCR is an opportunity to address this imbalance and reform forward looking charges significantly, making them form the bulk of network charges and thereby making the network much more cost reflective and ready for greater flexibility. If this comes to pass, then the residual charges will truly be a 'top-up' as intended and make the perceived problems in residual charging far less important. In this scenario, the expected benefits of the TCR may be much smaller than anticipated.

For this reason, we would encourage Ofgem to delay this TCR until the outcome of the SCR is known. If forward looking charges are changed this will impact residual charging and therefore the impact assessments carried out in this consultation will no longer be valid. It may even be the case that the reason for calling the TCR in the first place has been effectively dealt with by returning residual charges to their intended role as a small, relatively inconsequential payment.

We set out our response to the consultation questions below and look forward to further engagement in the consultation.

Yours sincerely,

Tom Cowling

General Counsel

Response to Consultation Questions

1. Do you agree that residual charges should be levied on final demand only?

Yes, we would support residual charges being levied on final demand only to remove distortions suffered by energy storage. Potentially this raises some questions over BSUoS charges where it's unknown which elements of the charge should be considered as residual or forward looking. We would encourage Ofgem to carry out an impact assessment into this issue and refresh other BSUoS related assessments in this TCR once the Balancing Services Charges Task Force has reported back with it's recommendations.

2. Do you agree with how we have assessed the impacts of the changes we have considered against the principles? If you disagree with our assessment, please provide evidence for your reasoning.

Not entirely, we do not agree that the minded to approach of Fixed Charges for consumers should have scored higher for Fairness than the Agreed Capacity charge approach. In table 6 all the points listed under Fairness for the Agreed Capacity charge were positive, while at least one of the points for Fixed Charges related to a perceived unfairness caused by the distributional impact within segments.

Furthermore, while it was argued that Fixed charges appear fairer by making charges the same for all, this is only true within user segments. The Fixed charges approach does recognise the need to scale the charges to user size or type but only partially achieves this aim by creating segments. Agreed Capacity charges provide the best reflection of user size, so we would argue that this is the Fairest option and should be Ofgem's minded to position in preference to the Fixed Charges.

Finally, concerns were raised by some at the Charging Futures Forum 15/01/2019 that LLFCs are not a suitable means to create segments and so Fixed Charges may not

[1] Ofgem, Targeted Charging Review: a consultation 13 March 2017. https://www.ofgem.gov.uk/system/files/docs/2017/03/tcr-consultation-final-13-march-2017.pdf

be as practical as presented in the consultation. In the detailed assessment of Table 7, we would suggest the Fixed charges options should be yellow for each category and the Agreed Capacity charge should be green for each category. We're unconvinced that dividing customers based on LLFC is as Simple, Transparent, Justifiable or Predictable as presented in the table. Few users will be familiar with the concept of LLFC and may find it confusing. Charges are set by everyone else's actual usage, so it may give the sense of the charge being inflicted upon customers outside of their control, making it less transparent and less justified. The charge will be quite predictable but based on sector volumes surely cannot be as predictable as a fixed deemed band as in the Agreed Capacity Charge?

3. For each user, residual charges are currently based on the costs of the voltage level of the network to which a user is connected and the higher voltage levels of the network, but not from lower voltage levels below the user's connection. At this stage, we are not proposing changes to this aspect of the current arrangements. Are there other approaches that would better meet our TCR principles reducing harmful distortions, fairness and proportionality and practical considerations?

Without having conducted our own analysis of this concern it is difficult to form a view, but it could be argued that electricity networks become more stable the larger they are and therefore all users benefit from the added stability brought by users at all voltage levels. If this is the case, it's not clear why residual charges should not include the costs of lower voltage levels. If one of Ofgem's objectives is to ensure a level playing field shouldn't all users pay for the whole network equally and not have the largest users getting a discount? This distortion could incentivise inefficient behaviour.

4. As explained in paragraphs 4.41, 4.43, 4.46, 4.49, 4.80, we think we should prioritise equality within charging segments and equity across all segments. Do you agree that it is fair for all users in the same segment to pay the same charge, and the manner in which we have set the segments? If not, do you know of another approach with available data which would address this issue? Please provide evidence to support your answer.

No, we would argue in favour of equity both within and across all segments. In the above mentioned paragraphs, we cannot see any reasoning as to why equality should be prioritised over Equity, rather the opposite. Paragraph 4.49 points out that under the equality approach within charging segments there will be winners and loser compared to the status quo, with larger users in each segment having the most to gain and the smallest losing out. This will leave the largest in each segment with an artificial competitive advantage and leave the smallest clamouring to be reclassified into the segment below. What is the reasoning for wanting to segment users in the first place? Creating arbitrary discrete segments invariably leads to undesirable distortions and so we would urge that this approach is abandoned and that charges fall across all users based on capacity. In our view fairness is best achieved with a priority on equity and would therefore favour the Agreed Capacity charge approach rather than Fixed Charges. As mentioned in our response to 2 there is also some concern whether LLFC is an appropriate method to set the segments.

5. Do you agree that similar customers with and without on-site generation should pay the same residual charges? Should both types of users face the same residual charge for their Line Loss Factor Class (LLFC)?

No, we would argue that customers with on-site generation are not similar to those without. Their interaction with the network will be quite different. Customers who have on-site generation are less dependent on the network and this should be reflected in how they pay for it. LLFC does not consider capacity or volume of import from the network and so there could be a broad range of users within each LLFC. Having a broad range within each LLFC segment creates winners and losers across the segment based on where the boundaries happen to have been drawn.

6. Do you know of any reasons why the expected consumer benefits from our leading options might not materialise?

It's important to note that not all customers benefit from this change, in particular domestic-low consumption customers which the analysis shows will see costs rise by £20 a year. It seems perverse that those customers who are perhaps least able to afford higher energy bills and/or have taken steps to reduce their exposure to ever rising network charges should now be penalised. Meanwhile, customers with high energy use are rewarded with paying less for the network. This relates to the issues raised in our opening response of not including energy efficiency as a principle in the TCR.

Expected consumer benefits may not materialise if consumer behaviour is significantly altered by these changes. We could expect a higher national peak demand if the incentive to avoid it is removed. This could add to wholesale and system costs while tightening supply margins.
Later in the TCR the analysis centres on the consumer benefits under two FES scenarios, Steady Progression and Community Renewables. The benefits of change were higher under Community Renewables, but because this TCR has been conducted without carbon reduction as a central principle, the unintended consequence of these changes is to reduce the likelihood of the Community Renewables scenario ever coming to pass. Even the Steady Progression scenario could be called into question with the damage to investor confidence leading to slow or no progression.

7. Do you agree that our leading options will be more practical to implement than other options?

In our view the Agreed Capacity Charge is the most practical to implement. It is the simplest to present as a single charge per kW capacity and with the arrival of smart metering determining capacity accurately for all users should become viable. We would argue that the Fixed Charges approach is not so simple as presented. LLFC's are not well understood by most customers and if they were it may result in undesirable outcomes of users applying to switch to a different LLFC with lower charges. E.g. Switch from Economy 7 to standard rate in search of lower network charges at the expense of energy efficiency and network price signals from the dual rate tariff.

8. Do you agree with the approaches set out for banding (either LLFC or demanding for agreed capacity)? If not please provide evidence as why different approaches to banding would better facilitate the TCR principles.

As mentioned previously we would argue that demand for the Agreed Capacity charge best facilitates the TCR principles and does so more effectively than LLFC does under the Fixed charges. The fixed segment approach of using LLFC in our view would not be as simple, transparent, justifiable, equitable or predictable than the Agreed Capacity charge. We do not see the need to segment customers discretely at all when a continuous alternative is available.

9. Do you agree that LLFCs are a sensible way to segment residual charges? If not, are there other existing classifications that should be considered in more detail?

No, we believe there are weaknesses to the LLFC approach and think customers will find it more confusing than a capacity based charge. Furthermore, we would argue against the need to segment the charges at all. It is more equitable and justifiable to base the charges on individual customers rather than trying to fit them into one size fits all segments.

10. Do you agree with the conclusions we have drawn from our assessment of the following? a) distributional modelling b) the distributional impacts of the options c) our wider system modelling d) how we have interpreted the wider system modelling? Please be specific which assessment you agree/disagree with.

Unfortunately, due to the number of significant industry changes ongoing at this time we have not had sufficient time or resource to review the modelling in sufficient detail to form a response.

We would suggest that these assessments be conducted again once other reviews and task forces which have a material impact on these assessments have reached their conclusion. This TCR can then conclude its decision on an informed basis.

11. Do you agree with our proposed approach to the reform of the remaining non-locational Embedded Benefits?

No, as discussed in our opening response, we feel this is the wrong time to be making further changes to embedded benefits while the SCR into Access and Forward Looking Charges is underway. The materiality of the current situation and of any changes made will be directly affected by the SCR and will alter the outcome of any impact assessments conducted so far.

12. Do you agree with our proposal not to address any other remaining Embedded Benefits at this stage? Which of the embedded benefits do you think should be removed as outlined in xx? Please state your reasoning and provide evidence to support your answer.

As set out in paragraphs 6.5 and 6.8 of the consultation, the reason for addressing some Embedded Benefits and not others was determined by their value and hence their ability to create significant distortions. Similarly, to our opening response and response to question 11, we believe this is the wrong time to make this assessment. If the Access and Forward Looking Charges SCR makes significant changes to the charging regime and the proportion of charges that fall as either FLC or residual charges, then this assessment will need to be made again and will possibly result in different or no Embedded Benefits being considered for review.

13. Are there any reasons we have not included that mean that the remaining Embedded Benefits should be maintained?

Remaining Embedded Benefits should be maintained until the outcome of the SCR is known. The industry will then be able to properly assess the impacts of the status quo compared to any changes.

14. Do you agree with our proposed approach to transitional arrangements for reforms to: a) transmission and distribution residual charges b) non-locational Embedded Benefits? Please provide evidence to indicate why different arrangements would be more appropriate.

We would encourage Ofgem to first delay a decision until after the SCR is complete and then consider a delayed implementation until 2023 to allow the industry to adjust to the new regime. The growth in network charges has been observed for some time so may well have been factored into business models for historic investment decisions, especially those related to flexibility such as DSR or storage or parties involved in the Capacity Market.

For those that didn’t account for embedded benefits in their investment decisions, it is still going to be an unexpected impact if these former benefits become a charge instead. Allowing time to adjust will alleviate any shocks to the market.

15. Do you agree with our minded to decision set out? If not please state your reasoning and provide evidence to support your answer.

No, we would oppose a segment-specific fixed charges approach as arbitrary segmentation will create distortions. The alternative proposal of Agreed Capacity charging would in our view be the most consistent with the TCR principles. We would encourage Ofgem to delay a decision on this until after the outcome of the SCR is known and then to consider phased implementation once the impacts are fully understood.

Similarly, for the most significant remaining non-locational Embedded benefits, the future significance of these can only be understood after any significant changes form the SCR and the Balancing Services Charges Task Force are known.

16. For our preferred option do you think there are practical consideration or difficulties that we have not taken account of? Please provide evidence to support your answer.

Yes, besides our opposition to segmentation we're not convinced that using LLFC's is a practical method to segment consumers as this was not what LLFC was designed for. We would consider this approach to be less simple, transparent, justifiable, equitable and predictable than the Agreed Capacity charge on offer.