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Andrew Self
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Office of Gas and Electricity Markets (Ofgem)
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By email to: TCR@ofgem.gov.uk

04 February 2019

Dear Mr Self,

Response to consultation "Targeted charging review: minded to decision and draft impact assessment"

Falck Renewables Wind Ltd has three UK offices located in London, Bellshill and Inverness. It is the UK subsidiary of Falck Renewables SpA ("Falck"), which is a publicly listed Italian company based in Milan. The company is active in a range of renewable energy technologies (onshore wind, solar, biomass and waste to energy generation) and has a 1GW portfolio operating in Italy, Spain, France, USA and the UK.

In the UK, Falck's assets and interests are currently represented by 12 onshore wind farms (installed capacity ~413MW). Ten of the projects are located in Scotland, with one of each of the remaining two being located in England and Wales. Falck's two largest assets, the Kilbraur and Millennium Wind Farms are both connected at 132kV to the Scottish transmission network. With a combined installed capacity of 133MW, they represent a third of the portfolio (by installed capacity). The remaining assets range in size from ~11MW to ~59MW and are embedded within the Scottish, English and Welsh distribution networks.

We are taking this opportunity to respond to Ofgem's **Targeted charging review: minded to decision and draft impact assessment consultation** ("TCR consultation"); our key points are set out below and responses to specific consultation questions are contained in Annex One. This response is marked confidential as some information specific to our business is included in the document.

The outcome of this consultation and any changes that are implemented will impact the future landscape of the GB electricity market, which in turn is key to on-going financial viability of both new and existing renewable energy schemes.

The creation of a smart, flexible electricity with long-term stability needs the application of consistent regulation and policy making to ensure long-term objectives are met in an efficient manner. Without an environment like this, which will allow renewable schemes to flourish subsidy free, both existing and new renewable schemes will be impacted. As a result, decarbonisation targets will not be met, and consumers will pay more for electricity generated from expensive fossil fuel generation. The worst outcome could be a reduction in installed renewable generation capacity rather than growth.

To create an environment in which investors have confidence to bring new renewable schemes into operation:

- There must be effective and coordinated regulation which starts with aligned high-level principles across a number of stakeholders (e.g. Ofgem, BEIS). Proposals in the TCR consultation represent a small part and should be considered within a long-term approach.
- Stability over future costs for current and potential projects is needed – implemented changes must provide a stable, transparent and fair future charging regime. TCR consultation proposals do not align with this and some may be subject to further change within the near future.
- The timeframe for change must balance the needs and activities of all relevant parties (consumers, generators and their investors and system operators) so that they can contribute to the evolution of a smart, flexible electricity system. Changes should be based on fact and analysis to justify changes and it is not clear this is the case in the TCR with respect to BSUoS while a task force looks at this matter at the same time

Without the right environment, it is possible that existing projects will cease to be viable, resulting in closure and new projects may be put at risk. Some technologies (e.g. on-shore wind) are slowly becoming viable without subsidy in certain circumstances, but the TCR consultation proposals may make this impossible; they will certainly hinder this outcome and likely delay the point at which other technologies become viable without subsidy. These outcomes are undesirable for consumers both in terms of cost and the failure to achieve carbon targets.

We do not support the proposals for change in the TCR consultation that affect generators because they will adversely affect distributed renewable generation. They will not facilitate an environment that will deliver significant volumes of cheap low-carbon generation and as a result will not deliver for consumers in the long-term. In addition, we believe the proposed changes, which adversely affect existing projects as well as new ones, do not comply with Article 6 of the European Union Renewable Energy Directive II which states that "support granted to renewable energy projects are not revised in a way that negatively affects the rights conferred thereunder and undermines the economic viability of projects that already benefit from support".

The TCR consultation process is not aligned nor joined up with other relevant aspects of regulation and potential changes. In particular, Ofgem launched a Significant Code Review (SCR) in December 2018 (Electricity Network Access and Forward-Looking Charging Review)[1] and asked the Electricity System Operator (ESO) to lead a task force (the Balancing Services Charges Task Force)[2] to review the costs of electricity system balancing.

Some aspects of the TCR consultation proposals relate to charges which are being reviewed by these two workstreams. It is inappropriate for Ofgem to issue a "minded to" decision under the TCR Consultation without allowing the other reviews to complete and all the facts to become available. Ofgem's decision to publish the TCR consultation at this point in time appears illogical, damaging and poorly thought through. For example, it seems inappropriate to force through a change in BSUoS when changes to align other cost recovery mechanisms across distribution and transmission networks are not introduced at the same time.

The outcome of the other reviews could see TCR Consultation proposals, if implemented, reversed soon after. This would be damaging for renewable generators, not only in terms of established

[1] https://www.ofgem.gov.uk/system/files/docs/2018/12/scr_launch_statement.pdf
[2] https://www.ofgem.gov.uk/system/files/docs/2018/11/decision_to_launch_a_balancing_services_charges_taskforce.pdf

plant revenue/ cost streams but also in relation to investor confidence for future schemes. Ultimately consumers will pay more as a result of a reduced number of cheap low-carbon generation schemes.

The timelines proposed in the TCR Consultation do not balance the desired outcomes with the ability of affected parties to respond and deliver; in simple terms they are too short. Implementing such significant changes to future revenue/ cost streams requires a much longer notice than proposed. Without this, existing projects will not be able to put in place appropriate mitigating measures and currently viable plant will be forced to close.

This will damage investor confidence in the sector. Given the other reviews and the possibility of one or more TCR Consultation proposals being reversed, investors and projects are, at best, likely to be delayed and at worst abandoned, as investors find opportunities with less regulatory risk in other markets or sectors.

Generators of all sizes will be adversely affected by the changes proposed regardless of where on the network they are connected. Generators currently paying transmission residual charges will see costs rise if these are removed as they are negative and therefore provide a benefit. Other generators in receipt of BSUoS-related revenues will see a reduction in revenue if this aspect is removed, along with a concurrent increase to costs as they become subject to a BSUoS charge. Although some larger generators can access the Capacity Market (CM) or the Contract for Difference schemes, this category of smaller generators cannot. They will be the backbone of low-carbon delivery and future investment is in jeopardy because of these changes.

Potential new and currently operating schemes will have to assess the overall effect of the changes, which will reduce the viability of each scheme. The impact could be up to £5.00/MWh due to changes in BSUoS alone, i.e. up to 10%[3]. [confidential material removed]

We are pleased to see that Ofgem has decided to extend the small generator discount[4] until March 2021. However, we would ask you to include the issue that this temporarily addresses as part of the overall charging review. This will help to ensure that there is an enduring solution and a smooth transition when the latest extension comes to an end. Early visibility of the regime from April 2021 is essential to ensure projects are not put at risk through sharp changes to charge levels.

In summary our view is that the sensible course of action is for Ofgem to **halt the TCR consultation process pending completion of the Balancing Services Charging Task Force and the Electricity Network Access and Forward-Looking Charging Review SCR**.

A short delay provides Ofgem with a window to consider the TCR Consultation proposals in conjunction with any recommendations from the other reviews and ensure that collectively they deliver the best overall outcome for consumers. It would enable one consolidated set of proposals, covering all charging aspects, to be consulted on and, if appropriate, implemented; this would be more efficient for everyone involved.

Publishing minded to decisions, especially where there is potential for them to be reversed or superseded by subsequent regulation is at best unhelpful and at worst puts at risk the flexible, cheap and reliable low-carbon electricity system of the future.

Please do not hesitate to get in touch if you have any questions about our response or would like to discuss the contents further.

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[3] This figure relates to energy generated and is therefore indicative of unsubsidised project revenue. Some projects may receive other sources of revenue (e.g. via sale of renewable obligation certificates), although it cannot be assumed that these additional revenue sources will be available for the lifetime of the project

[4] https://www.ofgem.gov.uk/system/files/docs/2019/01/sgd_decision_letter_final.pdf

Yours sincerely

R. S. Dibley

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Annex One – Consultation Questions

In this annex, we have set out in more detail out responses to specific consultation questions.

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

   Although we understand Ofgem's aims in this area, we are concerned that the approach to implementing this policy does not take full account of how different groups of network users, particularly generators, are impacted as a result of the change from current arrangements. The timeframe and abrupt nature of the change do not afford generators sufficient options for action to minimise the impact on their business and achieve a sustainable future.

   For example, to achieve Ofgem's preferred policy, transmission network residual charges must be removed from generators. This will be detrimental to large transmission-connected generation; as this charge is currently negative, they will see an immediate cost increase (our response to question 11 below comments in more detail).

   Section 4.3 of the TCR Consultation indicates that it is acceptable for costs on generation to be passed to consumers in the long run, but in the short-term generators will be adversely impacted as the timeframe for change is too quick. There are no transitional arrangements that allow the impact on affected parties to be minimised (e.g. through phasing).

   If the implementation is to avoid damaging existing projects (which may result in closure) and affecting potential new ones, there must be sufficient and appropriate transitional arrangements.

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.**

   By considering making TCR Consultation proposals in isolation, you have not considered how these aspects of charging interact with those being reviewed elsewhere. As a result, you are not able to judge and reach appropriate conclusions on whether:

   - harmful distortions may be introduced in other areas or at a later point in time;
   - the proposals are fair to all parties on an enduring basis – other review outcomes may be at odds with TCR Consultation proposals; and
   - the TCR Consultation proposals are practical/ proportionate or whether a change would be more practical/ proportionate if implemented in combination with a proposed outcome from one of the other reviews.

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?**

   We have no specific comments in relation to this question as we are not active in retail supply and do not have any final demand customers.

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.**

   We have no specific comments in relation to this question as we are not active in retail supply and do not have any final demand customers

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)?**

   We have no specific comments in relation to this question as we are not active in retail supply and do not have any final demand customers.

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

   The proposed changes as set out in the TCR consultation will be very damaging for existing and future low-carbon generation in the future. Not only will this adversely affect future low-carbon generation projects, but it will also call into question the financial viability of future projects to revamp / repower projects with the potential to force assets off the system earlier than expected.

   Neither of these is in the interest of consumers as they will not benefit from the provision of low-cost, low carbon generation.

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

   Although you consider the implementation of your options to be feasible from an industry process/ regulatory perspective, the timeframes proposed do not allow those most affected (whether distributed renewable generators or consumers) to adequately plan and/ or put in place mitigating actions. In the long-term, the outcome could be harmful for consumers and cost more through reduced investment in low-carbon renewable generation projects and the failure of existing schemes.

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

   We have no comment in relation to this question.

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?**

   We have no comment in relation to this question.

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.

We have no comment in relation to this question.

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

No, we do not agree with Ofgem's proposed approach to reform remaining non-locational Embedded Benefits (i.e. transmission generation residual charges, how balancing services charges are recovered and the removing the small generator discount).

Transmission residual charges for large generators are currently negative. The TCR Consultation proposal to remove them will result in a rise in TNUoS charge and therefore a cost increase for large, transmission-connected generators.

Although Ofgem considers that this will reduce the overall cost for consumers (TCR consultation paragraph 6.15) it does not appear that the degree of impact to large, particularly renewable, generators has been fully considered or whether they may consequently close in the future. Some, but not all, generators are able to access the Capacity Market and Contracts for Difference schemes. They may seek additional revenue via these to cover increased TNUoS costs and as a result the cost to consumers of these schemes may rise, negating any benefit derived for consumers from the change to transmission residual charges.

Further, the interaction of the TNUoS charge calculation, resulting from this change, with EU regulation 838/2010[5] which limits transmission charges to a €2.50/MWh annual average should have been considered and presented in detail as part of the TCR Consultation proposals. Although we note that the ESO has been asked to develop a suitable modification for the implementation of this change, it is not acceptable to publish a minded-to decision without setting out how the resulting framework will operate and be compliant with current legislation and impacts of Brexit.

[Confidential material removed]

In relation to balancing services, the ESO-led Balancing Services Charges Task Force will not report its findings until May 2019. It is key that the split between forward-looking vs. residual cost elements within the overall BSUoS charge is established. Without this, a consistent approach to cost recovery across different networks and costs (i.e. forward-looking vs. residual) cannot be implemented by network operators.

In reaching its proposed reforms for the recovery of balancing services charges set out in this TCR Consultation, you cannot have considered issues that will be identified and raised by the Task Force. Further Ofgem cannot have considered how any TCR Consultation reforms would complement, reinforce or replace any remedies suggested by the Task Force. Progressing any changes as proposed by the TCR Consultation now, could result in further change proposals within a few months. This is inefficient, unnecessary and is already creating additional regulatory uncertainty.

[5] https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:250:0005:0011:EN:PDF

Removal of the BSUoS Embedded Benefit from suppliers and introducing a BSUoS charge to small generators will result in significant additional cost to both existing and new projects and will alter the viability of many.

[confidential material removed]

This change seeks to address a perceived defect. Changes to current BSUoS charging mechanism and regimes should not be proposed until the Balancing Services Charges Task Force has completed its review and documented any recommendations. As part of this work, a technical market study is needed to establish whether recent upward trends in BSUoS levels can be attributed to smaller [renewable] generation that is connected to the distribution network. If this is not demonstrated to be the case, any proposed changes should seek to recover costs elsewhere.

We welcome Ofgem's decision to modify standard licence condition C13 of the electricity transmission licence[6], published on 24 January 2019. This will extend the discount for small generators in Scotland from 31 March 2019 to 31 March 2021 and is encouraging for those generators that are impacted, particularly low-carbon, renewable technologies. However, we are concerned that the lack of clarity around next steps is creating uncertainty because the distortion in charging between Scotland and England & Wales may not be properly addressed for the long-term; this uncertainty can be avoided by acting now.

Setting out now how further review will be dealt with allows this valuable aspect of charging to be considered within the wider charging landscape. An enduring solution that provides a positive charging framework for small transmission-connected generators in Scotland is more likely to be found if a piecemeal approach to regulation in this area is avoided.

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.

Yes, we agree.

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

Before making any further proposals, you should allow the other workstreams to complete their reviews and report their findings.

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 are not in agreement with Ofgem's approach to transitional arrangements for either transmission and distribution residual charges or non-location Embedded Benefits.

Aside from the proposed changes themselves, the timeline does not align well with the business horizons that affected renewable generation owners and investors operate in. Many embedded generators have contractual arrangement in place for the sale of power for three to five and sometimes up to seven years in advance. The short timeframe proposed will mean many

6 https://www.ofgem.gov.uk/system/files/docs/2019/01/sgd_decision_letter_final.pdf

arrangements will need to be revisited unnecessarily; a longer timeframe would be less disruptive for all parties.

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

We do not agree with the minded to decision set out in the consultation document. In our opinion it has been reached prematurely and has not been supported by a robust, appropriate and timely regulatory process. Not only are the timings of the TCR Consultation and other workstreams not aligned, but you have directed that some industry changes being pursued under standard industry change processes be stopped[7] while others could still progress[8]. Although you have determined that the proposal set out in CMP308 is outside the scope of the Balancing Services Charges Task Force[9], you have only suggested that work be stopped. The establishment of the Task Force presented an opportunity to bring together all relevant Balancing Services Charges work under one umbrella with a single source of output and recommendations. A firmer stance on your part would have resulted in efficient and joined up thinking.

Various aspects of network charging are currently under consideration, in particular network access and future charges are being reviewed under a significant code review (SCR) launched in December 2018 (Electricity Network Access and Forward-Looking Charging Review) and the costs of electricity system balancing are being reviewed by the Balancing Services Charges Task Force. Conclusions from these workstreams will not conclude until autumn 2020 and May 2019 respectively. In reaching the minded to decision, you cannot have considered how any proposals or issues identified by these significant workstreams could impact the TCR Consultation proposals. This is creating further unnecessary regulatory uncertainty **now** because of the possibility of further change.

We have serious concerns over the disjointed approach to network charging that is evolving. The associated uncertainty is dampening investor confidence. Without a holistic approach to all aspects, it is not possible to set out and implement proposals that meet the over-arching principles you have set out in the TCR Consultation.

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.**

We have outlined our views on the TCR Consultation proposals and challenges above.

[7] For example, https://www.ofgem.gov.uk/system/files/docs/2018/11/cmp302.pdf and https://www.ofgem.gov.uk/system/files/docs/2018/10/cmp307_direction_letter.pdf

[8] For example, https://www.nationalgrideso.com/codes/connection-and-use-system-code-cusc/modifications/cmp308-removal-bsuos-charges-generation and https://www.nationalgrideso.com/codes/connection-and-use-system-code-cusc/modifications/creation-new-generator-tnuos-demand-tariff

[9] https://www.ofgem.gov.uk/system/files/docs/2018/11/cmp308_letter_on_continuation_of_the_mod.pdf