

CMP308 – Minded-to decision and draft impact assessment

ENGIE response to the Consultation

Background to ENGIE

In the UK, ENGIE owns First Hydro Company in a 75/25 JV with Brookfield Renewable Partners. First Hydro Company comprises 2088MW of pumped hydro generation at two sites, Dinorwig (6 units each of 288MW capacity) and Ffestiniog (4 units each of 90MW capacity), both in North Wales. ENGIE also operates a UK retail business supplying gas and electricity to I&C customers.

Key points

- ENGIE agrees with Ofgem’s “minded to” position on CMP 308 as it will increase efficiency and competition in the wholesale market to the overall benefit of consumers.
- The implementation date should be April 2023; the industry has been considering this change for many years and Ofgem’s approach to reform (both the principles and the specifics of CMP308) have been signalled to the market for a long time. There has been adequate time to prepare and there is no need for further delay.

Questions

1. Do you agree with our assessment that CMP308 better facilitates the Applicable CUSC Objectives?

Yes, the assessment given in the consultation document is well balanced. It is clear that the key benefit is that CMP308 better facilitates competition (objective (a)) as it removes distortions between classes of generators.

2. Do you agree that charging BSUoS charges only to Final Demand reduces distortions between Large Generators and other forms of generation? Please explain why.

Yes, we agree. There is no economic basis for the different treatment of classes of generators as regards BSUoS charging, rather this difference can only distort the market and reduce the efficiency of price formation. This distortion impacts wholesale prices in the short and long term as it influences both dispatch decisions and investment decisions. Further, as it inefficiently incentivises generators to locate at the distribution network level then there is an impact on the required network investment

and/or constraint costs. The current arrangements are unnecessarily inefficient. The distortions are well set out in the consultation and were explored thoroughly in the two BSUoS Taskforce reports and the LCP analysis.

3. Do you have any views on the impact of this proposal on Behind The Meter Generation and its competitiveness?

The CMP308 impact on the BTMG distortion seems likely to be small. We agree with the approach given on page 29 of the consultation that this distortion can be monitored after CMP308 is implemented and further action taken as required (the charging regime should not be a driver of inefficient investment decisions). We would expect this distortion to be addressed at some point.

4. Do you have any views on our reasoning on this proposal's effect on price signals or generation dispatch?

An estimate of the expected BSUoS cost will be included in the BSUoS-liable generators' dispatch decisions; removing a volatile, unpredictable charge will remove any risk premia being applied currently. Further, by allowing greater competition between classes of generators it will result in a more efficient dispatch of the generation fleet and interconnector flows. It is clear that BSUoS is a cost recovery charge and, as such, the most economically efficient action is to apply it to Final Demand.

5. Do you have any views on our reasoning on this proposal's effect on competition between different generator types?

The reasoning in the consultation is sound.

6. Do you have views on our assessment of the decarbonisation impacts of this proposal, both in respect of emissions from the GB energy system and of overall emissions?

The consultation is reasonable.

7. Do you have views on whether and the extent to which the changes proposed in this modification have already been incorporated into supplier decisions?

This potential change has been considered by the industry for several years. There have been multiple opportunities to engage in the process and the "minded-to" position from Ofgem has been well-signalled (both in terms of principles and the specifics of CMP308). Further, a long lead time has been signalled (April 2023). There has been ample time and opportunity for suppliers to consider the impacts of such a change and reflect it in their commercial arrangements.

8. Do you have views on the impact of this proposal on existing supply contracts, including the possibility of costs or delayed benefits to consumers stemming from windfall gains to industry parties, or double payments?

This proposal has already had a long lead time which should minimise the risk of such theoretical gains/ losses. The known distortion has been allowed to persist for a long time so as to facilitate a robust consideration of the issues (two Taskforces, minded-to documents, substantial quantitative

analysis, long lead times for implementation in CMP308). The consultation identifies significant savings to consumers (and wider societal benefits) and there seem to be no reason for further delay.

9. Do you have views on this proposal's impacts on generator and supplier risks, including on exposure to volatile charges?

Clearly, it would reduce the risk of volatile charges for that class of generators who are liable for BSUoS currently (it would have no impact on those generators who do not pay BSUoS currently); if certain generators are no longer liable for BSUoS then this reduction in the expected cost of production (including any risk premia) will be reflected in wholesale prices.

10. Do you have views on the interactions between this proposal and other changes in the sector, including other BSUoS charging reform proposals?

It is consistent with the other reforms in the charging arrangements (and it would be inconsistent with those reforms to reject CMP308).

11. Do you have views on the modelled assessment of consumer and energy system benefits? Please provide quantitative analysis and any further information.

No.

12. Is our assessment of non-monetised costs and benefits reasonable? Are there any other factors we should consider?

It is reasonable.

13. Do you consider the consumer and system benefits identified in our consultants' modelling to represent a reasonable view of the potential effects of this modification?

The modelling seems to be thorough.

14. Do you consider that Ofgem has duly considered all relevant consumer and system benefits? Are there any areas which could benefit from further analysis?

No, the analysis is thorough and there have been a significant opportunity for the industry to engage in the modelling. There is no need for further analysis.

15. Our modelling assumes that CfD adjustment payments designed to compensate contract holders for the BSUoS charges they face will no longer be paid in the event generation is not liable for BSUoS charges. Do you agree with this assumption, and do you have views on our assessment of the risks associated with existing CfD contracts?

We agree with the assumption: the key point is to establish the most efficient market. If there is an anomaly in the CfD subsidy arrangements, then this anomaly should be worked through as rapidly as possible. There does not seem to be a reason to think that this cannot be resolved. This anomaly is not a reason in itself to delay the establishment of the most efficient market possible.

16. Do you have views on the impacts of this proposal on end consumers, including large users and vulnerable users?

Overall, the most efficient market possible will benefit all consumers in the long run. BSUoS costs are transparent to many non-domestic consumers particularly those on pass-through contracts and that the implementation of CMP 308 will increase the significance of these costs, in effect transferring the cost to a wholly direct cost on the consumer bill rather than half of the cost being inbuilt into the wholesale price. It is important, given the increased transparency that the concurrent modifications CMP361/362 are implemented alongside CMP308 to help with predictability and budgeting for consumers and to reduce the price risk for suppliers when setting fixed prices for consumers.

17. Do you agree with our assessment that reduced costs to generators are likely to feed through into lower wholesale prices?

A reduction in generators' cost will feed through into the wholesale prices. The GB generation market is competitive (see CMA's report of 2016¹) with no generator having unilateral market power; there is no reason to expect such a cost reduction will not be reflected in the wholesale market prices.

18. Do you agree with our assessment that this policy will not have any significant material impacts on vulnerable users?

The consultation is reasonable.

19. Do you agree with our assessment that this modification is unlikely to lead to any significant impacts on essential services or supply chains?

The consultation is reasonable.

20. We would note that increases in demand costs will need to be incorporated into the Price Cap methodology. Do you have any views on this area?

The consultation is reasonable.

21. Do you agree with our proposed implementation date of 1 April 2023? Please provide your reasoning.

Yes. This potential change has been considered by the industry for several years. There have been multiple opportunities to engage in the process and the "minded-to" position from Ofgem has been well-signalled (both in terms of principles and the specifics of CMP308). Further, a long lead time has been signalled (April 2023). There has been ample time and opportunity for suppliers to consider the impacts of such a change and reflect it in their commercial arrangements. Any further delay simply results in known market distortions being allowed to persist, thereby reducing the overall market efficiency unnecessarily.

¹ <https://assets.publishing.service.gov.uk/media/576c23e4ed915d622c000087/Energy-final-report-summary.pdf>

22. Do you have any other information which is relevant to this consultation?

No.

For further information, please contact

Andy Rimmer

Commercial Optimisation Manager

GEM UK

andrew.rimmer@engie.com

11th January 2022.