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Dear Mark,

RESPONSE TO OFGEM'S ELECTRICITY DISTRIBUTION PRICE CONTROL & STRUCTURE OF DISTRIBUTION CHARGES CONSULTATIONS

The RPA has produced this response jointly with the Combined Heat and Power Association.

The Renewable Power Association is a trade association representing producers of renewable energy. It is pan-technology – its members are involved in all forms of renewable energy, including biomass, wind energy, solar, biogas, energy-from-waste, landfill gas, hydropower, wave, tidal stream and sewage gas. The RPA has over 200 members and together these account for the lions share of renewable energy capacity.

The Combined Heat and Power Association works to promote the wider use of combined heat and power and community heating. Clean and efficient Combined Heat and Power (CHP) is already in use on close to 1,500 locations around the UK.

This combined response therefore represents the views of a large number of embedded generators.

We hope you find it helpful in your deliberations.

Yours sincerely,

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Director of Policy
Renewable Power Association

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Head of Research
Combined Heat & Power Association

Introduction

- 1.1 The Renewable Power Association (RPA) and the Combined Heat & Power Association (CHPA) welcome the prominence afforded to distributed generation in the Electricity Distribution Price Control Policy document of March 2004 and the Structure of Electricity Distribution Charges Update document of April 2004.
- 1.2 Both regulatory documents consider issues impacting upon the charging arrangements for distributed generators in future. Significant interdependencies exist between the two documents with different aspects of the proposed Generator Distribution Use of System (GDUoS) charging arrangements being contained within each.
- 1.3 For completeness, the RPA and CHPA have chosen to combine their responses to the Price Control and Structure of Charges consultations in order to capture our comments on the proposed regulatory developments, relating to distributed generation, within a single document.
- 1.4 In principle, the RPA and CHPA support Ofgem's proposals to move from the current Deep connection charging arrangements to an approach based upon 'Shallowish' connection charges with the coincident introduction of GDUoS charges.
- 1.5 The RPA and CHPA also support the introduction of a capacity related incentive to encourage DNOs to proactively connect increased numbers of distributed generators to their networks although we have a number of concerns regarding the latest proposals as outlined below.

2. DISTRIBUTION PRICE CONTROL: DISTRIBUTED GENERATION & USE OF SYSTEM CHARGES

Rates of Return & Cost Recovery Mechanisms

- 2.1 The proposed incentive scheme will enable DNOs to earn increased rates of return when connecting distributed generation. Whilst this should encourage proactive DNO behaviours, we remained concerned that distributed generators will be required to fund these revenues increases alone. The RPA & CHPA strongly believe that any increased rates of return should be apportioned equally across both demand and generation customers (Paragraph 5.16).
- 2.2 The RPA and CHPA welcome the proposals to reallocate any potential under recovery of pass-through costs to demand customers (Paragraph 5.20).
- 2.3 The RPA and CHPA regard the asymmetric cap and collar arrangements to be unduly generous towards DNOs. Whilst the collar limits DNO downside exposures to their cost of debt, the proposed cap arrangement allows DNOs to earn twice their cost of capital. Obviously, charges based upon such proposals could prove onerous to distributed generators, especially if there is no apportionment with demand customers (Paragraphs 5.30).
- 2.4 The RPA and CHPA seek clarification regarding the commencement date of DNO GDUoS revenues relative to the completion date of connection works. Paragraph

5.15 implies that DNOs will be entitled to revenue 'as costs are incurred' whereas Paragraph 5.26 states that revenues can commence 'once the generating capacity connects'. The RPA and CHPA strongly support the principle that GDUoS charges should only commence following the successful completion of the generation connection.

Capacity based incentives

- 2.5 Clarification is sought regarding the rationale for the proposed incentive rate (£1.50/kW/year) being based upon a Shallow connection charging methodology rather than the Shallowish approach as advocated in earlier consultations. The impact of this inconsistency will be to artificially limit DNO exposures to under recovery (an increased proportion of connection assets will be funded via connection and the pass through component of GDUoS charges) whilst simultaneously increasing the overall rate of return for DNOs connecting large volumes of distributed generation. The net effect of this inconsistency, assuming a Shallowish connection charging regime is adopted, will be to disadvantage distributed generators through the imposition of higher than necessary GDUoS charges. (Paragraph 5.22 and Table 5.1).
- 2.6 The RPA & CHPA agree that the allowance for the Operation and Maintenance (O&M) should relate to all connection assets (sole use and shared assets) although Ofgem's 'rounding up' proposal, from £82/kW to £100/kW, appears to represent an arbitrary (22%) increase which will result in increased O&M costs for distributed generators (Paragraph 5.24).

Depreciation Timescales

- 2.7 The RPA and CHPA are particularly concerned by Ofgem's selection of a 15 year depreciation timeframe for network infrastructure associated with distributed generation. This assumption is inconsistent with the approach adopted for Demand related infrastructure even though the assets employed are clearly comparable. Both the RPA & CHPA would expect the asset lives associated with both demand and distributed generation network infrastructure to be aligned (consistent with the approach to connection boundaries). Our preference would be to adopt a 40-year time horizon, consistent with transmission assets (Paragraph 5.27) .
- 2.8 Whilst the RPA & CHPA support Ofgem's position regarding the duration of the incentives (excluding O&M) being aligned with asset depreciation timescales, both consultation documents are silent regarding the equivalent treatment of the pass-through elements underpinning GDUoS charges. The RPA and CHPA seek confirmation that both the incentive and pass-through elements will cease after the assets have been depreciated, as the costs of connection would have been fully recovered. Such an approach would result in distributed generators with fully depreciated connection assets only paying charges corresponding to O&M (Paragraph 5.27).
- 2.9 Confirmation is also sought that existing generators already connected to distribution networks, having paid deep connection charges, will not become liable for the payment of GDUoS charges in future.

Incentives for ongoing network access

- 2.10 The RPA & CHPA welcome the introduction of incentives for the ongoing provision of network access to distributed generators although continue to regard the proposed incentive rate of £0.002/kW/hr as derisory (Paragraph 5.39)
- 2.11 As generators will effectively be paying for firm access rights, the RPA & CHPA believe that the proposed incentive should apply in all circumstances of network unavailability and should not be conditional upon the operating status of the generator. Network unavailability represents the loss of an option to generate. (Paragraph 5.39)

Volatility of GDUoS Charges

- 2.12 A key factor influencing the development of distributed generation projects relates to financial uncertainty. Unpredictable GDUoS charges would exacerbate such uncertainties and thus reduce project attractiveness. There is a risk that highly volatile GDUoS charges, based upon Shallowish connections, may prove less attractive to developers than the current Deep arrangements. Consequently the RPA & CHPA urge Ofgem to adopt the cost recovery approach which maximises GDUoS stability as confirmed through financial modelling (Paragraph 5.40).

3. STRUCTURE OF ELECTRICITY DISTRIBUTION CHARGES CONSULTATION

Connection Boundary Guidelines and Apportionment Rules

- 3.1 The RPA and CHPA support the proposals to establish a common connection boundary for generation and demand. Similarly, the removal of the 25% allocation rule for reinforcement cost apportionment is also welcomed.
- 3.2 The RPA and CHPA have concerns regarding the draft guidelines for connection charging boundary rules (Paragraph 3.8 & Appendix 2). It is our understanding that the apportionment rules remain under discussion at the Distribution Charging Implementation Steering Group (ISG) and the apportionment formulae included in these guidelines do not yet have the full support of all ISG members.
- 3.3 Within these connection charging guidelines, the 3x multiplier in the fault level apportionment rule is of particular concern to the RPA and CHPA. Fault level considerations can have a significant impact upon the solutions adopted for distributed generation connections. The apportionment rule as drafted increases the distributed generator's fault level contribution by a factor of 3, which can significantly increase their share of reinforcement costs. The technical justification for this multiplier has been requested on numerous occasions, yet an adequate explanation has yet to be provided. Until such an explanation is forthcoming, the RPA and CHPA will continue to regard this apportionment rule as unreasonable (Appendix 2).
- 3.4 Whilst the RPA and CHPA support Ofgem's proposal that DNO should retain the value of network assets displaced as part of network reinforcement, we seek confirmation that any network reinforcement charges to distributed generators will have such values offset accordingly (Paragraph 3.22).

GDUoS Charging Structure and Incentives

- 3.5 See comments 1.4 – 2.8 above.

Volatility of GDUoS Charges

- 3.6 In addition to 2.12 above concerning the requirement to minimise GDUoS tariff volatility, the RPA & CHPA support Ofgem's proposals regarding the adoption of tariff caps or alternatively tariff increase restrictions (Paragraph 3.32). We will continue to monitor developments in this area through the ISG.

Billing Issues

- 3.7 The RPA & CHPA support Ofgem's proposals to enable distributed generators to have a direct contractual (Use of System) relationship with DNOs outside the current Supplier Hub arrangements. Whilst such a proposal is welcome, we remain concerned that insufficient work has been undertaken facilitate such direct contractual relationships from April 2005 (Paragraph 3.33).
- 3.8 Similarly, the RPA and CHP are concerned that timescales for the introduction of the Shallowish charging arrangements remain challenging. Consequently, we would appreciate sight of each DNO's indicative DUoS tariffs at the earliest possible opportunity with corresponding worked examples demonstrating the method of calculation.

Power Factor

- 3.9 The RPA and CHPA recognise there can be cost implications to DNOs of variations in customer power factors. We welcome Ofgem's guidance that any associated DNO charges should be cost reflective. Indeed, in situations where generators were able to reduce DNO costs through the provision of reactive power, it would be reasonable for such generators to be rewarded accordingly (Paragraph 3.36).

Contestable Connections

- 3.10 The RPA and CHPA support the requirement on DNOs to provide a breakdown of the contestable and non-contestable elements of connection charges (Paragraph 3.36).

It is clear that the regulatory arrangements for distributed generation have progressed significantly in recent months. The RPA and CHPA will continue to contribute to the development of short and long-term solutions to distribution network charging issues, including the ISG. Should you require any clarification regarding any of the issues contained within this document, please do not hesitate to contact Gaynor Hartnell or Syed Ahmed at the RPA and CHPA respectively.