CHEMICAL INDUSTRIES
ASSOCIATION

STRUCTURE OF ELECTRICITY DISTRIBUTION CHARGES CONSULTATION ON THE LONGER TERM CHARGING FRAMEWORK

Response by the Chemical Industries Association

The CIA welcomes the opportunity to respond to this important consultation. The CIA shares Ofgem's views that any use of system (UoS) charging models should adopt the charging principles of: cost reflectivity, simplicity, transparency, predictability and facilitation of competition. Further we also agree with Ofgem that the new charging models that will replace the current distribution reinforcement model (DRM) should accurately reflect forward looking costs, incentivise efficient usage and development of the system, and incorporate the generation use of system charges (GDUoS). We would therefore urge Ofgem to uphold these core-charging values and ensure that they are applied to any Distribution Network Operator's (DNO's) methodology before it is approved. More specifically, the CIA would like to comment on the following areas:

Cost Drivers: The CIA agrees with Ofgem that it is essential for DNOs to identify their key cost drivers and incorporate them into their charging model. Whilst we also recognise that capacity will be a key cost driver the CIA would encourage Ofgem to ensure that all cost drivers are incorporated into the new charging methodologies in a simple and transparent manner. Further the CIA is firmly of the opinion that locational based charging would be beneficial to the development of the new charging models and are an essential element in providing both generators and consumers locational signals for investment.

NGC DC Load Flow (DCLF) Investment Cost Related Price (ICRP) Model: The CIA is unable to comment on the practical feasibility of implementing an ICRP-type model for DNO use. We recognise the advantage of this type of model in providing locational cost signals. However, if such a model were to be adopted it is essential that the core principles of simplicity and transparency be followed given that tariffs would be likely to vary year on year. It would therefore be essential that industry was provided with advance warnings of any step change in tariff level as early as possible, and that these step changes were transparent in order to provide confidence in the new model.

Line Loss Factors (LLFs): The CIA is concerned to learn that the methods used to calculate these factors are neither published nor audited. We therefore fully support Ofgem's proposal that this methodology should be more transparent, and therefore should be included within the charging methodology statements in the future. Again this should help to provide transparency and confidence in the calculation of these factors.

Demand and Generation Revenues: The CIA agrees with Ofgem that any distribution tariffs should be cost reflective. If these signals do incorporate locational elements in the future, the CIA would however be dismayed if the consumer continued to shoulder the whole burden. It is essential that these costs are shared with the generators to ensure that they too receive locational signals, as their siting decisions will have major impacts on distribution network costs.

Generator Charging Issues: The CIA is wary of any proposal that appears overly complex and costly, as its administration costs will ultimately be borne by the consumers. The CIA agrees with Ofgem's approach that in future all new distributed generators should face the same charges. However

we question the need for economic models and historic cost adjustment when dealing with generators who have already paid deep connection charges. We agree with Ofgem that these generators should not be charged twice for a product, but that they should pay for any costs from which they used to be exempt. CIA believes that if simple and transparent charging models were adopted, any additional costs that generators did not pay in their deep connection charges should be easily identifiable and therefore charged. We would strongly recommend that any solution adopted by Ofgem should follow the same charging principles as applied to the new charging models.

Ancillary Services and Active System Management: As stated previously Ofgem should seek solutions to problems that are in line with their charging principles applied to the new charging methodologies. Any solution that is not simple to implement and transparent should be rigorously examined to ensure the benefits of such a proposal outweigh the costs. The CIA is therefore dubious as to the full benefits of this proposal when compared to the costs and complexity of implementing it.

Reactive Power Charges: The CIA is unable to comment at this stage on Ofgem's proposal to seek to charge for the reactive power requirement of certain consumers. We would seek greater clarity on how these charges would be calculated, what impact they will have on different consumer classes and how the solution will be in line with Ofgem's charging principles. We would urge Ofgem to ensure that the methodology applied to the calculation of these charges is simple, transparent and cost reflective, and that any reactive power charges levied be clearly identified on consumers' bills.

Consistency between DNO Areas/Models: The CIA agrees with Ofgem that there will be a benefit in DNOs working together to provide consistent charging methodologies. We believe that the adoption of consistent charging models will reduce barriers to entry and aid competition within the electricity industry. Furthermore the adoption of consistent charging models should also aid transparency, simplicity and predictability as consumers and generators will not have to be familiar with numerous models when making their siting decisions.

Interaction Between Transmission and Distribution Charging: As one of Ofgem's stated objectives is cost reflectivity, the CIA believes that any behaviour that results in additional costs should be charged to the party causing that cost. If the actions of a party on the distribution network affect the costs imposed on the transmission network, then these costs should be reflected. How such a system would work in practice is not clear, but again the CIA affirms its support for the principles of simplicity and transparency.

If you have any queries regarding any of the comments raised in this response please contact Stefan Leedham (0207 963 6736).

CIA Credentials

The CIA is the leading representative and employers' body for the UK chemical industry, with 150 members at over 200 manufacturing sites. Within its membership there are a significant number of energy intensive - alongside smaller business - users of energy.

The chemical industry in the UK contributes over £5 billion annually to the country's balance of payments from a gross output of over £50bn in 2003. It accounts for 2% of UK GDP; 11% of manufacturing's gross value added; employs some 230,000 highly skilled people directly and supports several hundred thousand jobs throughout the economy nationwide. It also provides a contribution of almost £5 billion to the UK national Government and local authorities and invests some £3.5 billion on R&D.

The industry is one of the most energy intensive sectors of the economy accounting for 6% of the nation's gas and electric consumption, and is manufacturing's largest consumer of energy at 22%. In addition to its consumption of energy for heat and power generation, the industry uses energy directly in many chemical processes, as well as using hydrocarbons as raw materials in the manufacture of basic petrochemicals and fertilisers.

The chemical industry is heavily reliant on gas for its own electricity generation requirements. . The industry now generates around 30% of its own electricity, most of which is from Combined Heat and Power Plants (CHP). These plants have helped to contribute to the industry's continuing energy efficiency improvements.