

Fourth DEWG meeting

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| Minutes from the fourth DE working group meeting. | From | Victoria Arr | 25 October 2007 |
| | Date and time of Meeting | 16 October 2007 Fourth DE Working Group meeting | |
| | Location | Ofgem | |

Attendees

| Name | Organisation | Name | Organisation |
|-----------------|-------------------------|-----------------|--------------|
| Malcolm Taylor | AEP | Robert Tudway | LCCA |
| Neil Feinson | BERR | Allan Jones | LCCA |
| Rita Wadey | BERR | Stephen Andrews | Lowerwatts |
| Stephen DeSouza | BERR | John Costyn | OCC |
| David Miller | CE Electric | Philip Davies | Ofgem |
| Claire Walsh | Centrica | Rachel Fletcher | Ofgem |
| Graham Meeks | CHPA | Vanja Munerati | Ofgem |
| Neil Witney | DEFRA | John Kemp | Ofgem |
| Dan Meredith | E.ON UK | Ijaz Rasool | Ofgem |
| Matthew Nunn | EDF Energy | Victoria Arr | Ofgem |
| Roger Barnard | EDF Energy | Duncan Mills | Ofgem |
| Richard Lee | Future Energy Yorkshire | Cherie Davis | Ofgem |
| Chris Welby | Good Energy | Terry Ballard | RWEnpower |

Apologies

| Name | Organisation | Name | Organisation |
|-------------------|--------------------|--------------------|-----------------|
| Ralph Chamberlain | E.ON UK | Steve Armitage | Smartest Energy |
| Dave Sowden | Micropower Council | Katherine Marshall | SSE |
| Frank Malley | Scottish Power | Robert Hackland | SSE |

Summary of discussion

Introductory remarks and purpose of meeting

- Philip Davies introduced the group to its fourth meeting, the purpose of which was to debate the proposed measures set out in Discussion Paper 3: Supply Licensing and Exemptions.
- It was noted that, since the previous meeting, Ofgem had continued to meet with market participants to discuss their views on the problems and barriers affecting DE schemes. However, the focus of the work had now moved towards the exploration of potential solutions as summarised in the Discussion Paper. Members of the Working Group were encouraged to provide their comments on these proposals.
- It was suggested that the fourth working group meeting should be the final one, unless any members had any further issues that they wished to be raised, in order to ensure that it was possible to publish the consultation document in November. One member suggested that a final meeting in November could be useful in order to take a draft of the consultation document to the group. However, other members saw no need to hold a further meeting.

Discussion Paper 3: Supply licensing and exemptions

- Rachel Fletcher presented some slides outlining the main themes of Discussion Paper 3. It was suggested that the four key challenges facing DE schemes were scale, the cost of market and regulatory arrangements, the costs of becoming a licensed supplier and the costs and risks of operating in a competitive market. Working Group members were asked for their comments on whether they felt that this was a fair summary of the main issues.
- One member suggested that although electricity supply was a high volume, low margin industry, distributed energy schemes should be able to increase these margins. Another member commented that the issue of scale might be over-emphasised as the number of customers required to make a supplier viable was closer to 20,000 rather than the several hundred thousand assumed in the discussion paper. The key problem lay in the need to move risks from suppliers to a third party, as at the moment the high level of balancing risk made it difficult to obtain finance. Currently, there was seen to be a high 'hassle factor' associated with being a DE scheme.
- Another member commented on the fact that the introduction of new building regulations was likely to lead to a situation where suppliers would not be able to operate on specific sites unless they were using a specific type of energy. This could potentially create large numbers of communities who would not in practice be free to choose their energy supplier.
- One member raised the issue of site definition and how this affected the value of electricity to different parties. John Kemp ran through the arguments around VoE under different settings and explained his view that the difference in value in different settings reflected differences in costs.
- There was also some debate about Figure 2 in the discussion paper – 'Operating costs of a small licensed supplier (5MW)'. Members questioned whether the values given for various different costs were correct and if Ofgem had carried out (or was planning) analysis to clarify these costs. One member stated that there was a need to assess both whether these cost estimates are accurate and if the different types of costs are justified or not (ie, if it is fair/economically efficient for DE schemes to face these costs). Philip Davies said that Ofgem would do the best it can in the time available.
- Members also asked if this meant that small suppliers should be sheltered from the market-place in some way, and if this was the case, whether this should apply to all small suppliers or just DE schemes.

Raising exemption limits

- The Discussion Paper noted that one potential solution was to increase exemption limits, as discussed in previous workgroup meetings. It was suggested that any such increase should be accompanied by the imposition of additional conditions such as requiring DE schemes to register for exemption or limiting the number of customers outside the market. The group was asked for their views on this as well as on the issues that this could raise in terms of consumer protection, whether the increased limits should apply to all suppliers or just DE schemes, and whether they should apply to licensed suppliers.
- One member questioned whether the idea of raising the exemption limit was irrelevant, as the same result could be achieved through the licensing system. Another member expressed concern that introducing a requirement to register for exemption would increase the amount of paperwork associated with DE schemes. Increasing the amount

of consumer protection for customers of exempt suppliers would also mean that there was little difference between being an exempt and licensed supplier. One member also questioned whether the idea of a time-limited exemption period would make it more difficult for a scheme to obtain long-term finance.

- Another working group member raised the issue of whether it would be feasible to introduce such a system in the timeframe under consideration – the main advantage of the exemption approach is that it can be implemented quickly. However, other members felt that changes to the license arrangements could be implemented relatively quickly if necessary. It was felt that, if this was the case, there was little point in increasing the exemption limit as a 'quick-fix' solution would be unnecessary.
- One member felt that there was no need to make any changes to the existing distribution license system.
- Another member also questioned whether raising the exemption limit without amending the RO could create a problem for some DE schemes who might not be able to receive ROCs.

Becoming a licensed supplier

- Rachel Fletcher noted that the DEWG had also considered how the benefits of being an exempt supplier might be replicated within the licensing framework. Options could include: delegation of certain aspects of the Supply license to third party agents, ensuring the provision of agency services in the market, introducing a threshold for the RO, preventing customer switching for a period of time and removing the option of exemption for DE schemes to encourage the market for agency services. Working group members were asked for their comments on these potential measures.
- One member questioned whether the aim of the consultation was to find a solution just for the next few years, or something that would work in the longer term. Ideally, the solution proposed would be a long term one, however the small number of DE schemes in existence at the moment made it difficult to identify exactly what the issues are, and therefore further revisions may be required. It was also noted that it was unclear how enduring the current issues were going to be, since technological change may produce solutions in future.
- Another member suggested that it would be helpful if the consultation document outlined which option was preferred, and how long this would take to implement.
- There was some debate regarding the issue of agency services. A working group member noted that third party agency services were already available, but that many schemes were unwilling to pay for them. In particular balancing services were expensive due to the risks of high costs associated with a high cash-out price. There was also an issue of scale, in that these services were most expensive for the smallest suppliers. It was emphasized that there was a requirement for trading, pricing, settlement and billing services for DE schemes regardless of the route to market. There was no way of avoiding this issue without changing the BSC to remove the risk to small suppliers. One member stated that there needed to be a regulated entity in the middle providing agency services if it was believed that this was in the public interest.
- Philip Davies reminded the group that Ofgem was in the process of reviewing Cash-out arrangements, and encouraged members of the group to contribute to this debate. It was also noted that anyone was able to raise a modification proposal, and that several small suppliers had done this in the past.
- One member commented that the trading arrangements for a low carbon electricity market would be very different to the current arrangements, and questioned whether

there was any mechanism to run a trial of the proposed system to demonstrate how it would work.

- A member stated that the valuation of embedded benefits in DUoS charges is a very important issue which impacts on the value of energy. He believed that this issue is no more technical than some others which are being covered in the consultation document.

Closing remarks and timeline

- Most members felt there was no need to hold a further meeting before the publication of the consultation document. Future meetings of the group would be held on an ad hoc basis, with the additional possibility of a workshop to be held near the end of the consultation period. There was also the option of having bilateral meetings.
- One member did not believe there was a vast array of views in the group, and that there was general consensus on the need to develop a new licence model. The member also expressed concern about the level of transparency regarding the discussions between Ofgem/BERR and LCCA on the consultation and particularly the cost estimates used in the analysis.
- Members were invited to give any written feedback on issues raised in today's meeting to Ofgem by Friday 26th October.

Actions

- 1. Send any comments on the issues raised in this meeting to Rachel Fletcher by 26 October.**