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Dear Anna,

Subject: Distributed Energy – Initial Proposals for More Flexible Market and Licensing Arrangements

Good Energy is a licensed electricity supplier of nearly 25,000 customers operating within England, Wales and Scotland and is currently applying for a gas supply licence. In addition we are working with several EDN consortiums developing low carbon distributed energy solutions, and therefore we welcome the opportunity to comment on the above consultation.

For your ease we have addressed the questions as set-out in the consultation expanding on our views as appropriate.

Chapter 2

If the exemption limits for supply and distribution to domestic customers were to be raised, what measures would be required to ensure ongoing and effective protection of energy customers, and how would this be enforced or monitored?

In principle, Good Energy is not against the raising of the threshold for domestic customers on an EDN in terms of exemption from a distribution licence. We also feel the limit should be in terms of customer numbers rather than a megawatt demand figure. Where the EDN has a licensed supplier providing top up and spill, then the supplier should undertake to ensure customers on the EDN which they are, in effect part supplying, pay no more than the tariff offered to adjacent customers within the GSP group in which the network is embedded. If the licenced supplier does not supply domestic customers outside the EDN, then a formula based on current offerings by other suppliers should be developed. Suppliers would then "back to back" this requirement into the top up & spill contract and enforcement could then be via the supply licence of that company.

In terms of the European directive, and dependant on the ECJ ruling, EDN operators could be required to allow customers to switch supplier. If this became so, then they should be allowed the flexibility as to how this is done rather than imposing the full weight of becoming a licensed network operator on them. Demonstration of this facility would be required prior to receiving exemption, and the regulator could be given powers to require the operator to seek a licence if it felt that the operator was impeding this facility.

Should the existing per company maximum exemption limit be removed allowing one company to develop a number of different sites?

Yes. In practice if this limit is of limited use as companies will just set up different subsidiary companies for each site to avoid this limitation. If distributed energy is to become part of the solution to meeting EU renewable targets then commercial firms need to operate in this area, and operate several sites under one company to achieve efficiencies.

We welcome evidence on the size of DE scheme that would be considered economic and efficient in different settings if exemption thresholds were not an issue. We also seek views on what the appropriate exemption limits should be across generation, supply and distribution.

We take the view that the exemption limits for generation and distribution should be based around their potential export/import connection to the local licensed network operator for the following reasons:

For Generation the limit exist to protect the network at both local and national level. A 10 MW generator which passes most of its generation through to a licensed network operator is of more concern than a 100MW generator where the energy is all used within the EDN. Therefore the exemption limit should be based on the capacity to export to the licensed network not on the capacity of the generator or generators within the EDN.

It is less clear why there is a limit on network exemption, other than a recognition that network operators provides a monopoly service, in which case no exemptions should apply. Clearly the licensed network that connects to the EDN has an interest in ensuring it has a proper connection agreement with the EDN based on the potential impact on its own infrastructure, but like generation this should be based on the capacity of the connection, not the actual energy used within the network.

On supply exemption, this is more based on consumer protection, as a customer supplied by an exempt supplier does not have either regulation or competition to protect them. If the EU directive requires EDN's to allow supply competition, then a limit would be nonsensical. If the concept of a monopoly supplier is allowed to exist on an EDN, then the exempt supplier will probably need a top-up and spill agreement with a licensed supplier where the EDN meets the licensed network, and it would make sense to put obligations on suppliers providing top up and spill which could be "back to backed" in the top up and spill contract. Hence a limit here would not be needed either.

We welcome views on the 2001 Class Exemption Order, and areas where there could be more clarity in particular.

Based on our answers above, we believe that consumer protection can be handled by either facilitating competition within a EDN, or by placing obligations on suppliers who provide top up and spill arrangements, which can be "back to backed" in contracts with the exempt supplier. It may be a requirement for an exempt supplier to have such a contract.

We also believe exemption limits on domestic customers should be abolished, but if maintained should be based on customer numbers rather than demand. Equally exemptions on generation and EDN's should be based on capacity connections to a licensed network.

Chapter 3

Do you consider it appropriate to use the provisions of the BSC to increase the representation of DE schemes in BSC governance processes?

No. The BSC governance panel has upon it Generators, network operators and supplier representatives, most of whom are not attached to any one particular market player. They also obliged to consider the industry as a whole, and no "bat" for their constituents when conducting business. It will be in the interest of suppliers providing top up and spill arrangements to ensure changes raised are suitable for their business in this area as they are the one exposed to the market risk.

We do think that in the area of DE there may be a conflict of interest for National Grid

Do you consider that there is a case for allocating funding for DE representation in BSC governance? If so, do you have views on where the funding should come from?

No. Small licensed players receive no such support. It would therefore be anti-competitive to provide funding to DE representatives, but not to provide support for licensed players. If you were to considering funding a position then it should cover all players below a certain size and make sure it represents their views.

Have we considered all the options to address the risk DE schemes are exposed to if trading in the wholesale markets? We welcome any other proposals to accommodate the needs of DE schemes selling their electricity in this way.

The proposals seem to be based on the problems DE providers have due to size. While we agree there are issues, they apply equally to small licensed suppliers such as Good Energy, and therefore any changes should address problems for both licensed and exempt small players. We believe that DE parties should link into the BSC trading arrangements via their provider of top up and spill as they are the ones who are facing the risks.

Chapter 4

Do you consider that third party purchasers undervalue exports from DE schemes? We would welcome information from both generators and purchasers on prices that have been agreed for electricity from small generators. If necessary, the information can be provided in confidence.

No. The market does discount energy that cannot be guaranteed to be delivered within a particular half hour, as it exposes market players to the unpredictability of cash out. However, this is not just a problem for DE operators but to all market players, in particular renewable generators and players without a balanced portfolio of generation and supply assets.

Good Energy purchases renewable energy from approx 350 small generators and in most cases find that we are not the only Supplier offering terms and end up making several bids of increasing magnitude to secure the output. On this evidence, we do not believe that generators are receiving anything less than full market price.

We would welcome views on whether there is a lack of competition in the market for small generator output?

As mentioned above, Good Energy buys from small generation output from hundreds of generators and often has to bid against other purchasers. We do not believe that there is a lack of competition. The market value for energy which is not predictable could be increased if the unpredictability or difference between SBP and SSP (see graph in appendix A) could be resolved, thus reducing the risk discount on prices. This however is an issue wider than DE, and needs to resolved to suit DE and the wider community.

Have we considered all the reasons for the lack of development of consolidation services in the market? We welcome views on whether further changes to the market rules may be warranted to remove any barriers to entry that continue to exist for consolidators.

The lack of consolidators is due to the illiquidity in the market. This in turn is due to the market being dominated by 6 vertically integrated companies, who self supply and only trade small amounts in the market. The driver to self supply is driven by the unpredictability of balancing prices, which poses greater risk to parties who are not in control of their balancing position. Lack of transparency in the wholesale market place and issues related to the balancing mechanism pricing is the key barrier to entry.

If balancing prices could be made more predictable, then this could open up the market for new entrants in licensed supply, DE and generation.

Do you think there is a case for a specialist Energy Trader? What are your views on the scope and functions the specialist agency could perform as an interface between DE generators and the current trading arrangements?

No. Supply companies are more than capable of offering top up and spill contracts. Most suppliers will offer these contracts, but DE participants feel the market prices offered are too low. A specialist trader will not improve this price. There are already traders in the market, they will offer product where there is a market/value for them to do so.

In Energy Trader option could be implemented by allowing the market to deliver, placing an obligation on suppliers or by tendering for the role. We welcome views on these suggested routes and any others we have not considered in this consultation document.

Good Energy is always willing to offer terms to DE schemes that are renewable, and we understand most other suppliers in the market are willing to do so. We would be against an obligation to offer terms purely on the grounds that we are a 100% renewable energy supplier and would have difficulty offering terms to DE based on carbon based generation. There is no problem with getting the oftake contracts, the key issue is the price. This returns again to the pricing of SBP and SSP and we would point OFGEM to look at the changes broad by NGC that undermine the value of variable generation in the marketplace.

Do you have any views on how the understanding and forecasting capability for DE technology could be improved?

No. Although accurate forecasting of renewable generation is a "Nirvana" many including Good Energy seek.

What are your views on the implementation of a dedicated wholesale market for DE?

This will make the current market more complicated, and if was implemented be open to small players generally not just those in the DE market. It would also probably be very illiquid – this solution doesn't appear to offer any real value in solving the problem. It sounds like a "policy" type solution rather than a practical one.

Resources would be better spent revising the existing cash-out mechanism and lack of market liquidity.

Have we considered all the options to address the lack of competition in the market for small generator output?

No. We disagree with the statement that there is a lack of competition for small generator output. There is an issue with the value of the energy because of the market mechanism creating risks, but it is a competitive market. Our experience is that the market for generator output is very competitive.

Chapter 5

DE schemes face a trade-off between carrying the cost and ongoing maintenance of a private wire network linking their sites, and the direct and indirect costs of using the licensed distribution network. We are keen to better understand circumstances that lead a scheme to favour the private wire option and how incentives vary depending on the distance of the second (or multiple) sites?

The conflict between private wire versus using a licensed distribution network is primarily one of capital investment versus connection costs and UoS charges for use of the licensed network. However, it also depends on getting planning permission to run private wires between sites, the availability of a local network, and several other factors, but as a rule of thumb, the further the distance between sites, the greater the incentive to use the local licensed network.

The biggest deterrent to using the local network for neighbouring sites is that they are often charged DUoS as if they are using the whole network, although in practice they are using no more than a few hundred metres for the short hop. I

Is there adequate availability of Exempt Supplier Services in the market place? If the demand for such services is likely to increase with expected development of DE, we welcome views on whether the market will respond appropriately or whether intervention is required to ensure the availability of these services.

Yes, although they may not always be recognized as such. Suppliers often buy the output from an embedded generator and supply another related site. They pay a price for the generation, and quote a price for supply. These may be related as part of the deal, but are seen as two contracts rather than a top up and spill arrangement.

Most suppliers will offer such services at a price which provides a margin and covers the risk to which they may be exposed. Availability at a price that makes the scheme economically viable is dependent on the market value of energy, which is at the mercy of international energy prices.

We welcome views on whether an Exempt Supplier Services obligation (similar to the former Standard Condition 53) should be imposed on all suppliers and whether any specific additional requirements are now necessary.

No. This will prevent suppliers offering innovative solutions to make DE work on a site by site basis. At Good Energy we would have concerns about such an obligation on two counts, One that we only deal with renewable energy and would find ourselves obliged to offer terms to "carbon sourced" generation. Secondly, as a small supplier we would be obliged to offer terms to large DE schemes that we could not financially manage.

We welcome views on the feasibility of Exempt Supplier Services being provided at system cost – i.e., merely the costs incurred by suppliers from third parties in registering meters, using the network, etc. Are there ways of integrating with supply systems such that Exempt Suppliers do not create any overhead on Supplier operations?

We do not believe this is feasible.

Is there a case for DE representation at the Energy Network Association working group examining the technical standards for connection? If so, do you have views on how representation might be funded?

As this is a technical matter which impacts DE, then we believe this would be a prudent step to take.

We welcome examples of where technical standards may be unduly onerous and discourage connection to the network for small generators.

This is outside our expertise.

We welcome views on the proposed options to improve the accessibility of the licensed network to DE schemes, and whether there are any other relevant options we have not considered.

Option 1 – We do not agree with this for the reasons stated above.
Option 2 – Whilst BMUs or VIMPANs may sound simple they would be complex to administer. There is nothing currently in the systems that prevent suppliers aggregating MPANs on this basis, although the full cost of network charges would need to be considered. Nor does it resolve top up and spill.
Option 3 – We would have no problem with this, although the question of competition does arise where only certain customers can benefit from these proposals.
Option 4 – Yes, but only in conjunction with option 5
Option 5 – Yes , but only in conjunction with option 4
Option 6 – We would expect this to take place anyway.

Chapter 6

What are the costs of start-up for small suppliers? What is the break-even point for small suppliers?

To become a fully licensed Supplier in the UK electricity market, would require start up funding of approx £0.5-2M depending on the type of supply. We estimate the breakeven point to be around 20,000 domestic customers or commercial equivalent, the crunch being the financing required between start-up and reaching breakeven point. However, the dominance of the big 6 vertically integrated companies, credit requirements, unpredictability of cash out prices, lack of competition in agency services are all barriers to new licensed suppliers.

Costs and breakeven point may be lower in the concept of DE, as the Supplier would start with a fixed customer base, and not have to include acquisition costs in start up. The additional costs of an already licensed supplier operating on behalf of an exempt network are minimal.

Do economics of CHP justify the additional investment over and above that of a boiler based system? What are the contexts where CHP might be chosen over heat-only schemes?

Whilst we fully support the principle of on-site CHP, we are not qualified to answer this question.

Is there a case for granting a limited number of supply licences to new entrant DE schemes that restrict customers switching to an alternative supplier for a period of, say, 5 years?

Possibly, but the same terms should be on offer to an existing licensed supplier who provides the top up and spill arrangements for the DE scheme.

We welcome views on what types of advice and information would usefully help DE schemes start up and interact with the wider electricity system, and who should provide this?

From our experience, there is plenty of information available to DE scheme operators. Many of the schemes currently being proposed have existing players as part of their consortium, and there are many industry consultants able to advise.

Ofgem may have a role to play, by offering clearer advise on exemptions on their web site as well as other useful advice. Elexon could also play a role with their "introduction to the market" seminars.

Do you consider that there is a case for a new DE supply license? If so, do you have views on its key terms? Please explain your reasoning in detail.

No. Most of the issues are related to the fact that DE suppliers are small players in the market. Why should they have less onerous license obligations than new suppliers in the main market? There may be areas where the existing supply licence has conditions which are only activated when the supplier reaches a certain size as already exist for CERT and payment measures.

We welcome views on the proposed options for reducing the costs of becoming a licensed supplier and any other options that we have not considered in this consultation document.

Option 1 - It is difficult to see an example in either the MRA or BSC where a supplier could pass of the obligation to another supplier, and if this is possible then bi-lateral commercial terms should be possible without the need to formalise this.

Option 3 – This option has already been attempted by Utility Link who acted as a licensed supplier for several other parties who did not have a licence. Utility Link went into administration in Jan 2006, which suggest this model will not work well. Unless the service provider had some special status which exempts them from the risks within the market, then the supplier of last resort would need to be amended to cover DE schemes. If the provider did have special status, then it would have an unfair competitive advantage over other suppliers.

Option 4 – This could be done, but on an assisting small licensed suppliers basis not as a DE supplier basis.

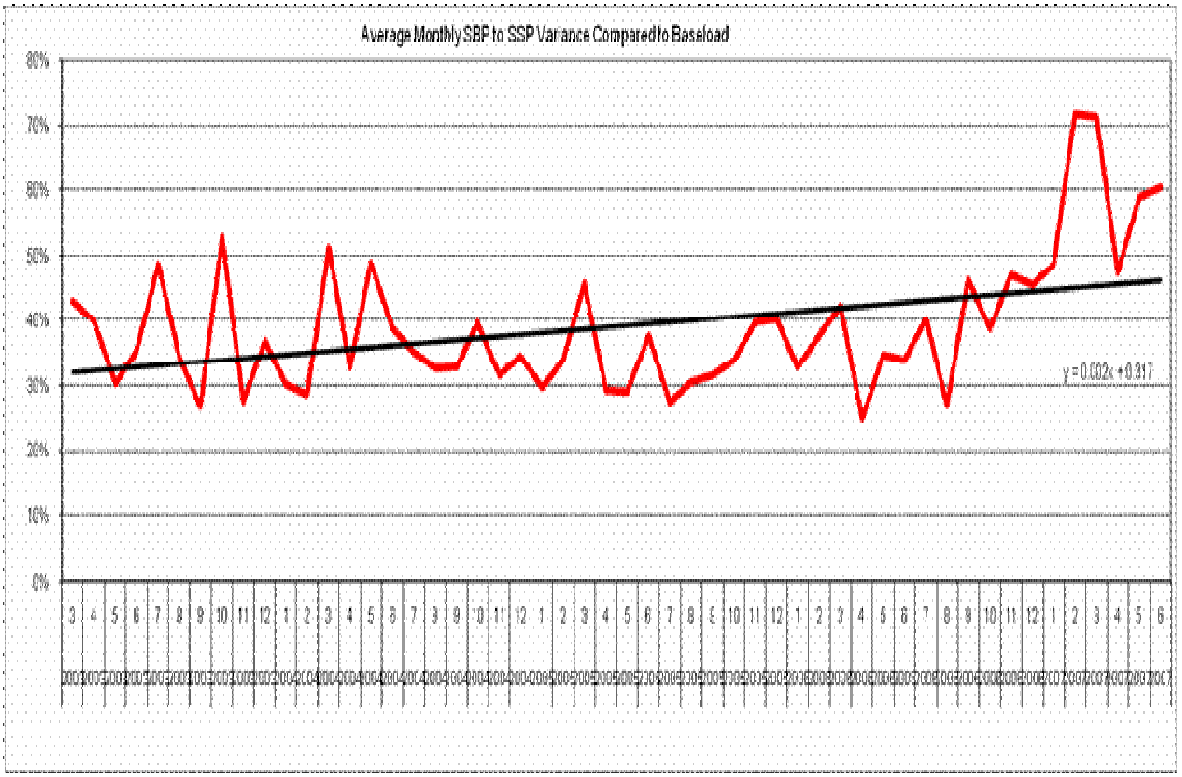
Option 5 – As mentioned in our answer to the previous question, it may be possible to review all licences to see if certain obligations can be laid dormant until a supplier reaches a certain size.

We hope that our comments are useful. If you have any questions about what has been discussed here, please feel free to contact us.

Regards,

Chris Welby
Commercial Director

Appendix A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70%
60%
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