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Dear Anna,

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

Thank you for the opportunity to respond to this consultation. We are supportive of Ofgem and BERR's efforts to promote the uptake of Distributed Energy (DE). However, we believe that the main barrier to the widespread uptake of DE is the lack of an economic support mechanism for heat. While some of the technical issues noted in the paper do raise concerns for DE, we consider that these are very much second order compared to the lack of an economic support mechanism for heat. As a consequence, no amount of reform to the detailed technical rules will significantly enhance the take-up of DE. Instead, we believe the first priority should be to put in place an appropriate support framework for heat. Indeed, we consider that DE is a subset of the heat market and with the right heat framework in place, DE would be able to operate within the existing licensed arrangements for electricity rather than as exempt.

The proposals in the consultation could be considered as simply tinkering with the existing electricity market arrangements. Whilst welcome, in the absence of heat support, they attempt to secure the benefits of being exempt whilst operating as licensed. However, that is neither an easy nor fitting task. We do not believe that the measures considered in the consultation e.g. consolidation, energy traders etc., would provide the level of support needed to allow DE to develop whilst licensed.

Fundamentally, in the current licensing framework, the economics of DE are and will continue to be challenging without some or other of: support for heat; the opportunity to access other support e.g. the Renewables Obligation; or access to the electricity exemption regime. In putting in place the exemption regime it is recognised that it is a balance between the benefits of facilitating small-scale generation through minimising overheads and regulatory obligations and protecting the interests of customers supplied by exempt participants. For DE schemes, the exemption regime allows

electricity market benefits to accrue to exempt DE schemes and these are used to support the heat element of these schemes, i.e. electricity is supporting heat. We have listed the benefits that being exempt brings in response to Question 16. These accrue even following the removal of the 28-day rule (e.g. there remains a risk and cost of legal challenge to longer-term contracts that does not exist with an exempt regime). These benefits of the exempt regime make it economic to develop DE. However, further growth in DE is being constrained by having to operate within the current exemption limits whilst there is no support for heat. This can only constrain the Government's achievement of its climate change targets.

As an interim solution, whilst waiting for a heat support and regulatory framework to be implemented, we believe that a small extension to the electricity licence exemption regime would allow the further development of DE schemes to continue. Once a heat support and regulatory framework is in place, DE schemes would be able to operate within the licensed arena, and it would therefore be appropriate to review the exemption regime at that time.

We do not believe that a new DE licence would be appropriate at this time, as it would be difficult to define and put in place, and would undoubtedly introduce additional costs and remove at least some of the benefits associated with exemption. Customer protection would be afforded through the existing Exemption Regulation provisions, even with a small interim extension to the exemption regime.

In conclusion, we believe that only a fully functioning heat support and regulatory framework will provide a sustainable solution for DE in the long-term. However, in the interim, a small extension to the licence exemption regime would provide a welcome, short-term but less sustainable solution until a proper heat support and regulatory framework is established.

We have provided our answers to the questions posed in the consultation in the attached confidential Annex. However these should be read in the context of the above, that we believe that the only sustainable way forward for DE schemes is through the implementation of a support and regulatory framework for heat.

We would be interested in attending the forthcoming industry workshops.

We hope that you find our comments helpful.

Yours sincerely

Rob McDonald
Director of Regulation