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17th June 2011

Dear Nicholas

Consultation on charges for pre-2005 distributed generators' use of DNOs' distribution systems - proposed guidance

The Association of Electricity Producers, Combined Heat and Power Association, Renewable Energy Association and RenewableUK wrote to you jointly on 13th August 2010, 5th July 2010 and 11th February 2010 giving our views on the proposals to charge Generation Distribution Use of System (GDUoS) for generators who connected before April 2005 when a deep connection charging regime applied. The associations (or their predecessors) have been engaged in this issue since 2005 and have held broadly consistent views on this matter over the last six years. For this submission Scottish Renewable Forum members also wish to acknowledge that they fully share our views.

We are again submitting a joint response to Ofgem's latest consultation to reinforce the fact that all significant trade associations representing the

generators that will be affected by these proposals have a common and united view on this issue. For the avoidance of doubt we are giving our views on behalf of both the generators that connected to a distribution network before April 2005 and those that connected after that date as well as many developers of generation projects that have yet to connect.

Our Position

We remain of the view that parties who connected prior to April 2005 under a regime where it was clearly the position that generators connecting to a distribution network paid deep connection charges but no GDUoS should be able to maintain that position. Retrospective regulatory changes of this kind midway through a project's lifecycle will not only impact upon the operational and financial viability of existing projects spanning numerous technologies but test investor confidence and threaten future commitment to new renewables projects.

Should parties be forced to pay GDUoS charges against their will then they must receive full compensation for this imposed change from the terms under which each site was connected i.e. the contractual agreement that they would not have to pay GDUoS charges after having paid deep connection charges. As a pragmatic and much simpler to implement version of the above, we proposed in August 2010 that the current arrangements, not having to pay GDUoS charges, should continue for a fixed period, being set for each pre April 2005 connected generator according to the following principles.

1. If the existing agreement stipulated contract duration then this should be used to define the period;

2. If 1 does not apply then, apart from special circumstances listed in 3 below, the period should be determined from the typical life of distribution network assets; or

3. In the case where generation plants are expected to have a life that exceeds the typical life of distribution assets the period would be set from that. For example, when building a hydro plant, a prospective builder is required by the Reservoirs Act to ensure that the installed pipeline has a 50 to 60 year lifespan. The proposal would be to deal with each such site on a case by case basis.

This proposal is relatively simple to implement and has the desired economic effect of subjecting all generators to GDUoS charges at about the time that they might be considering closure. Subjecting them to GDUoS charges before the time at which closure is being considered performs no useful economic purpose at all. There is a case for consideration that where customers have paid asset replacement charges these charges should be taken into account in calculating a revised asset life or refunded with interest.

We consider it telling that as far as we are aware no generator that connected to a distribution system after April 2005 has made any representation to Ofgem that they are being unfairly discriminated against by virtue of the current position of pre April 2005 connected generators.

In order to be constructive we continue with comments on the questions that you have specifically asked. The responses should all however be taken in the context that we think that your fundamental approach proposed is misguided, disproportionate and serves no useful economic purpose. In some cases it is also liable to be open to legal challenge.

If you would like to discuss any of these comments further please let any one of us know and whoever you contact will liaise as required with the other Trade Associations. Whatever your deliberations here we would appreciate a formal response to our proposals as set out originally in our letter to you on 13th August 2010.

Yours sincerely,

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Chief Executive
Renewable Energy Association

David Porter
Chief Executive
Association of Electricity Producers

Guy Nicholson
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Graham Meeks
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Appendix 1

Responses to consultation questions

CHAPTER: Three

Question 1: *Is our description and interpretation of historical charging arrangements (including connection and use of system agreements, charging statements, determinations, and regulatory precedents) complete and accurate? If not, please provide supporting evidence setting out any issues that you identify.*

We consider that your interpretation of the historical universal understanding of the charging arrangements is incomplete, misleading and in one instance inaccurate.

Clarity of position pre April 2005

It is clear to everybody that was in the industry at the time that the position for embedded generation connected prior to April 2005 was that it paid deep connection charges including capitalised O&M and did not pay any DUoS charges. If it connected at a point where it deferred the need for network reinforcement it received no credit for that. This is well supported by for example the government sponsored "Technical Guide for the connection of embedded generators to the Distribution Network" produced by Econnect and Ilex and published in November 1998.

Section 5.2 covers the "Basis of PES connection charges". Section 5.2.1 starts "In cases where work has to be done to modify an existing connection or to provide an entirely new one, some or all of this work will be done by the PES. Thus, some initial costs will be incurred. These costs are invariably charges to the developer up-front, as part of the connection charge. The PES will also incur costs associated with the operation, maintenance repair and replacement of the new or modified connection infrastructure. These operation and maintenance (O&M) costs must be considered in addition to the initial costs. O&M costs are often capitalised and charged to the developer up-front as part of the connection charge."

Section 5.3.1 states "although electricity demand customers pay both connection and use-of-system charges, embedded generators are exempt from the need to pay distribution use-of–system charges. This is because all the PES's costs associated with generator connections are recovered through the up-front connection charge together with any ongoing service charges."

Note that the above document was sponsored by the government to give guidance to potential generators as to amongst other things the charges that they might face. There is no mention of even a potential for DUoS charges to be levied.

We can also look at your own December 2000 Structure of Electricity Distribution Charges Initial Consultation Paper. Section 4.26 states:

"Embedded generators presently pay the full capital cost of connection to the local distribution system, including the costs of reinforcement across the system. They do not pay use of system charges on their exports."

We are also aware that some generators paid contributions for asset replacement in addition to the capital cost of the assets.

Was it reasonable to expect change?

If the possibility of introducing GDUoS charges for export had been considered we would have expected that generators would have pressed for clauses in their contracts that dealt with this possibility, in particular for example the issue of refunds for reinforcements that were paid for as part of connection charges. Also, the absence of clauses in many contracts giving specific rights to use the system indicates that the parties concerned understood that it was satisfactory to pay for a connection without a specific right to use the system because all parties took it as read (consistent for example with the government guidance quoted earlier) that connection automatically came with a right to use the system for export.

Indeed as is stated in the consultation, some contracts specifically give the generator the right to export up to the Maximum Export Capability. To say that this is an incomplete right because there is no obvious right to have the power conveyed to a particular location demonstrates confusion between physical flows (which is what DNO charges are for) and contractual flows (energy sales / power purchase contracts). Providing that you can export your power to the system, and separately your customers are entitled to take power off the system (and pay DUoS for the privilege), there is no other right relating to physical flows that is needed and therefore no need to pay for any other service that the DNO might provide.

In our view the many parties who were concerned with the agreements were not actually incompetent for omitting to provide for this eventuality in their agreements because it was a given that a right to use the system existed, and would continue to exist for export without additional payment above the deep connection charge. Everybody involved was therefore comfortable with no specific mention of the issue.

Misleading statement

In paragraph 3.17 of the consultation you state "That characterisation reflected the fact that DGs did not generally impose a material UoS cost on the network to trigger such a charge, such that they were not typically being so charged at the time. That is, where there was no cost, DGs were not under an obligation to pay for it."

That is true in the sense that were there where no reinforcement costs these were not included in the connection charges (although customer connection works were included in charges and these connection assets were gifted to the DNO with the DNO free to offer connections to other customers using these assets). However what is also true (but you have not stated) is that where there was a "material UoS cost" the DG was charged for it via paying for a deep reinforcement. In other words it was absolutely clear that deep reinforcement charges covered all extra costs imposed by the generator on the DNO and that there was no case for any further charges and there were no other costs to recover.

In summary, with the exception that pre April 2005 connected generators were not given a credit if their connection deferred DNO reinforcement, it is quite clear that deep connection charging was a substitute for paying GDUoS charges i.e. were paid instead of GDUoS charges. It is equally clear from what is and also what is not in particular connection contracts, as well as the government sponsored guide to connection of DG, that it was taken as read that deep connection charging was a substitute to liability for GDUoS charges for export and that there was no expectation that this could be changed in the future.

Question 2: *Do you agree with our rationale for only allowing refunds for instances of double payment to be funded through the price control?*

There are two aspects to this question. The first relates to what compensation should be paid to any generator that having connected under a deep connection charging regime is then forced to pay GDUoS charges. The other relates to what should be recoverable by a DNO through the price control.

We do not agree that no case has been made to remove the right of pre April 2005 connected generators to use the Distribution System without paying GDUoS charges. Irrespective of what the agreements do and do not say, the fact that in return for the payment of a deep connection charge such generators have been allowed to use the system without further charge, in some cases for several decades indicates that de facto they do have that right. When a generator connects to the distribution system it expects energy to flow across it to the relevant end consumer.

With regard to what is legitimate compensation (and therefore should be recoverable under the price control) we do not agree that this amounts merely to instances of double payment. As we have said earlier we think that pre April 2005 connected generators are entitled to compensation for the loss of their rights. As a pragmatic measure we have proposed that this is simplified by granting them exemption from GDUoS charges for a set period.

We firmly believe that a DNO should be able to recover through the price control arrangements any compensation paid to a generator that is legitimate compensation for changing the way that the generator is charged. However if

Ofgem accept our proposed model then there should be no need to consider creation of an overcomplicated compensation methodology.

Question 3: *Are there any other instances (beyond that of double payment) where refunds should be funded through the price control? If yes, please explain why these instances are appropriate and compatible with the regulatory regime as it has evolved over time.*

This is the same question as Question 2 above just asked in a different way we therefore re-iterate our points from the answer above.

Question 4: *Are there any other circumstances beyond capitalised O&M payments that may give rise to instances of double payment that should be reimbursed and funded through the price control? If yes, please explain why these instances are appropriate and compatible with the regulatory regime as it has evolved over time.*

Leaving aside that we do not agree that refunding double payments (as opposed to compensation for the loss of rights) is sufficient, our view is that any payment made in order to deliver deep reinforcement should be part of a refund of double payments. The only substantive argument that paying GDUoS (after having paid for a deep reinforcement) is not a double payment, is the conjecture (which we have no means of knowing is correct without access to asset registers) that items that were paid for via deep connection charges are not included in the asset base upon which DUoS is levied.

For the purposes of price control it was absolutely correct that whilst the deep reinforcement assets were paid for through connection charges they should remain outside the DUoS charging base so that the assets are not paid for twice. However, as a charging issue it is clear that if it is decided that assets that were paid for via connection charges are now as a general rule to be paid for via DUoS charges then these assets should be moved within the scope of the DUoS charging base and the parties that paid deep connection charges for them should have the amount refunded. It would be totally iniquitous to have the position where assets of a certain type are generally in the DUoS charging base and paid for by all DUoS payers whereas a subset of those assets that were paid for by some generators via deep connection charges are not in that charging base even if all generators pay GDUoS charges.

To use the analogy with the move to “plugs” for transmission connections (i.e. super shallow charging) it would be like suggesting that instead of what actually happened, parties that had paid up front for connection assets that were of a type that would generally become TNUoS funded assets should get no refund for those payments even though those who paid them would pay TNUoS charges on the same basis as those parties that had not paid for any connection assets (that changed to TNUoS funded assets) up front. One suspects that if this had been suggested there would have been significant disquiet and possibly some legal action. NGET (NGC) and Ofgem at the time recognised that this would be an

unfair situation and sensibly chose to offer refunds for those connection assets (that were of a class that would in general become TNUoS funded assets) that had been paid for up front and move their funding into the TNUoS charging base.

In other words, for consistency with the introduction of the plugs methodology, if parties are to be forced to pay GDUoS charges and they are to be compensated merely for what they have already paid (neither of which to we believe is satisfactory) then any reinforcement assets that were paid for via deep connection charges should be moved into the DUoS charging base and parties that paid for them up front should receive a refund. Alternatively, if our proposed model were to be adopted these assets could remain outside of the charging base as now.

Some generators have paid asset replacement charges in addition to deep connection charges. These charges were levied to provide a fund to replace the assets at the end of their life (as determined by the DNO/PES). There is no precedent for such charges under the current regulatory regime for customers either at transmission or distribution, with either import or export capacity. Therefore any monies paid under such a regime should be taken into account in the calculation of an exempt GDUoS period or refunded with interest.

Question 5: *Do you agree with our proposed approach to calculating refunds for unexpired capitalised O&M payments? Please suggest any improvements to the approach outlined and reasons for these.*

We agree with the proposed methodology for calculating the unexpired portion of capitalised O&M charges.

Question 6: *Where DNOs have entered into agreements that are/were inconsistent with regulatory practise (e.g. giving indefinite rights to use the system without further change or entering into contracts that cannot be freely modified) do you agree that any compensation required by virtue of these contracts should not be refunded through the price control?*

Our view remains firmly that rights to use the system without paying GDUoS charges were entirely consistent with regulatory practice and therefore where compensation is given by a DNO in exchange for giving up these rights it should be recoverable through the DNO's price control arrangements. The rights may have been implicit or explicit (for example the right to export up to the MEC) but it is clear from everything written at the time that all parties had a common understanding of the arrangements they had entered into. We do not therefore think that there should be any question of DNOs not being able to recover compensation where generators give up the right to use the system for export without paying GDUoS charges.

We do not understand the concept of contracts that cannot (or can) be freely modified. A contract is an agreement between two or more parties and can be modified by the agreement of all parties to it. It would not be an agreement at all

if either or both parties could modify it “freely” against the wishes of the other party. We suspect that you are actually referring to the provision in some contracts whereby if one party wants to modify it and the other does not agree with the proposal the matter can be referred to yourselves for a determination. That provision was in some contracts but not others, however only for the case where the DNO proposed a modification to the contract. More recently contracts have had the determination provision for changes proposed by either party. Given the variation in this provision in different connection contracts we do not think that it would be appropriate to say that a contract with no such clause somehow implied a negligent DNO who should therefore suffer financially as a result.

We consider it telling that as far as we are aware no generator that connected to a distribution system after April 2005 has made any representation to Ofgem that they are being unfairly discriminated against by virtue of the current position of pre April 2005 connected generators.

CHAPTER: Four

Question 1: *In general are our proposals for implementing the refund arrangements considered by this consultation appropriate? Is the level of detail we have provided sufficient to make our proposals clear and workable? Please outline any areas where you think more clarity/detail is required.*

From what we understand of your current proposals we believe that what you are proposing is unjust, economically damaging, disproportionate and open to legal challenge. In order to undertake a full and robust cost benefit analysis much more detail is required regarding the definition of applied relevant terms and decision regarding the charging methodology which DNOs are to eventually apply, which at present is far from clear.

We cannot suggest any improvements to the mechanics for implementing the arrangements that you have proposed. However, we do not agree with the implementation of this solution and instead would suggest consideration of the model which we outlined in our 13th August 2010 submission. A view on this approach would be much appreciated.

If Ofgem insist that its proposals are applied, we can only foresee a time consuming, resource intensive and expensive exercise which will requiring extensive bilateral discussions for each pre April 2005 connected embedded generator covering adjustment to contractual arrangements from up to several decades ago. The cost of this exercise will of course eventually fall upon the end consumer.

Question 2: *In the section on "Consistent application of principles", have we appropriately identified who is eligible for a refund? Do we need to provide any further areas of clarification? Which of the two options outlined for mixed sites (demand and generation) are appropriate?*

We agree with the idea that all parties should be treated consistently. However this objective will be difficult to fulfil given the possible emergence of different treatment due to variations in contract wording that were thought by all parties at the time to have no practical significance given the common understanding of how Distributed Generation was to be charged for the connection to and use of the Distribution networks.

For mixed sites (with similar levels of import and export) we think that the only method that has general applicability is option 1, given that it is possible that for some sites certain asset reinforcements were driven by import requirements whereas others were driven by export requirements.

We note that members who are not vertically integrated or who hold a long term PPA will face significantly more financial risk where renegotiating affected contracts. If Ofgem insist upon pursuing a change to the current long standing

arrangements we would urge consideration of our proposed alternative approach.

Question 3: *Are the evidence requirements set out in the chapter as necessary to support a case for refunding appropriate? Are they sufficiently robust to prevent ineligible claims for compensation being recovered through the price control? Are there additional or alternative assumptions that could be used for supporting a case for a refund?*

We think that it should additionally be incumbent on a DNO who wish to levy DUoS charges to provide evidence that this was contemplated as a possibility when the initial connection was made.

Question 4: *Is our approach to due process appropriate? Are there additional or alternative steps that should be incorporated?*

We cannot suggest any improvement to the mechanical process for implementing this misguided proposal but would observe that it will be extremely difficult for Ofgem to address concerns regarding its role as 'Judge, Jury and Executioner' during the high level of appeals that will emanate from application of these proposals.

Question 5: *We welcome views on how refunds should be paid and the details of implementation. In particular, should it be a one-off payment, a phased payment or a hybrid of the two? If a refund is not a one off-payment, over what time period should it be paid? Do you agree with our proposals for refunds that are not agreed by 1 April 2012?*

Members believe that a one off payment is cleaner and should be adopted if this approach is preferred over our proposed approach once court cases have been concluded. If Ofgem is minded to continue to introduce these charges, despite the serious concerns raised by industry, agreed charges should be gradually introduced following the full settlement of compensation to all sites for any upfront payments for reinforcement works, O&M or use of system charges. A stepped introduction of the charges will provide time for affected generators to put mechanisms in place to mitigate the impact of these charges and is an issue under consideration in the Ofgem consultation 67/11 on Electricity distribution charging methodologies: DNOs' proposals for the higher voltages.

Question 6: *Do you agree with the mechanics for allowing DNOs to recover refunds through the price control?*

No as we do not see that this exercise is necessary. There are other far simpler and less litigious solutions to this perceived problem. Our proposed solution for instance would not require an adjustment to the price controls and would only affect the size of the charging base.

Question 7: *Do you agree with our proposals for dispute resolution where DNOs and DGs cannot reach a settlement by 1 April 2012? How can we encourage DNOs and DGs to reach a timely settlement? In particular, should use of system charges in respect of the DG be logged up and back-billed once a refund has been settled on? If these DGs do not have these charges back-billed, how should these charges be recovered by the DNO from other customers?*

Given that in some cases the dispute resolution process may be out of the control of either Ofgem or the DNOs it is impractical to put a licence obligation on the DNOs to resolve all disputes by a specific time. We suggest that if it proves impossible to recover the costs from some parties that this is dealt with in the same way as any other over or under recovery of DUoS charges.

Appendix 2

Our 13th August 2010 Submission

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Nicholas Rubin
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13th August 2010

Dear Nicholas

Charges for pre-2005 Distributed Generators' use of Distribution Network Operators' (DNOs') distribution systems Ofgem Consultation 88/10

The Association of Electricity Producers[1], together with Renewable UK, wrote to you in February 2010 outlining concerns we had regarding Western Power Distribution's proposals in respect of changes to its EHV charging methodology

[1] The Association of Electricity Producers represents large, medium and small companies accounting for more than 95 per cent of the UK generating capacity, together with a number of businesses that provide equipment and services to the generating industry. Between them, the members embrace all of the generating technologies used commercially in the UK, from coal, gas and nuclear power, to a wide range of renewable sources of energy. RenewableUK (formerly the British Wind Energy Association (BWEA)) is the trade and professional body for the UK wind and marine renewables industries. Formed in 1978, and with 630 corporate members, RenewableUK is the leading renewable energy trade association in the UK, representing the large majority of the UK's wind, wave, and tidal energy companies. The REA is the industry association representing renewable energy producers. It is the largest renewable energy trade association in the UK and covers heat, transport fuels and biomethane injection as well as all forms of electricity generation. With over 100 members active across a range of technologies and markets the Combined Heat and Power Association (CHPA) is the leading advocate of an integrated approach to delivering low carbon and renewable energy services using combined heat and power and district heating.

for pre 2005 Distribution Connected Generation. Since then a number of our members participated in an Energy Networks Association workshop on this issue held 6th May 2010. The Association of Electricity Producers, Renewable UK and the Renewable Energy Association wrote to you in July 2010 raising issues about the proposed interim charging changes and reiterating the concerns we raised with you in our February letter

Following the withdrawal of the interim proposals Ofgem published its 21st July 2010 consultation on Charges for pre-2005 Distributed Generators' use of Distribution Network Operators distribution systems 88/10. The AEP organised a meeting of its members to consider a response to the consultation and subsequently discussed our proposals with Renewable UK, the Renewable Energy Association and the Combined Heat and Power Association. We wish to make you aware of the outcome of our deliberations

Our Preferred Approach

Association members believe that Ofgem should allow Distribution Network Operators and their Distribution Connected Generators to recognise and abide by the provisions within their existing bilaterally agreed contracts. The variability of the *outputs from the* different methodologies proposed in the consultation poses a significant commercial risk for generators *as they will be unable to compete on a level playing field.* However, should any of the 270 generators identified by Ofgem as being affected by the proposals, wish to transfer to the proposed methodology then, they should be given the option to do so. This would be a one-way move which could not be reversed should charges change in the future.

Those pre April 2005 distribution connected generators that do not opt to pay DUoS charges would continue under their existing contractual arrangements for X years from the date of their connection, the value of X being set as follows:

1. If the existing agreement stipulates duration this should obviously be used to define the term of the contractual right;

2. If 1 does not apply then, apart from special circumstances listed in 3 below, X should be determined from the typical life of distribution network assets; or

3. In the case where generation plants are expected to have a life that exceeds the typical life of distribution assets X would be set from that. For example, when building a hydro plant, a prospective builder is required by the Reservoirs Act to ensure that the installed pipeline has a 50 to 60 year lifespan. The proposal would be to deal with each such site on a case by case basis.

In this way all generators would see the effect of DUoS charges around the period when they may be considering closure, thus having the desired economic affect at the time when it is important.

Rationale

Regulatory Good Practice should seek to ensure that the time and expenditure incurred in resolving a suspected defect or anomaly is proportionate. This is clearly not being accomplished with regard to this matter. Ofgem, Distribution Network Operators and affected Generators are all spending significant time, resource and finance on this issue which is disproportionate to the alleged benefit this new approach is aiming to deliver.

If Ofgem adopts the proposed approach to grandfather rights then this removes a large amount of effort which will be required to work out appropriate compensation, thus avoiding the debate about where the additional Distribution Network Operator funding comes from and the subsequent raft of appeals which are bound to follow.

Ofgem Monitoring and Management

In order to ensure that the 270 identified generation sites are being treated appropriately, Ofgem should ensure that a register is created to record the treatment of all affected sites. This could be created and maintained by Ofgem itself or another appropriate body e.g. the Energy Networks Association. As a generator moves closer to the expiry date of any grandfathered rights, the register would be used to ensure that Ofgem is informed when a dialogue between a Distribution Network Operators, and their specific distribution connected generator, has begun and been subsequently concluded. The register would of course be confidential as it would hold records of a commercially sensitive nature.

Over time, as generators' grandfathered rights reach their expiry date, when the affected plant then moves over to its specific Distribution Network Operator's Generation Distribution Use of System charge, the register would reduce in size.

Should you have any questions please contact Barbara Vest, Head of Electricity Trading Association of Electricity producers on 07736 197 020, Guy Nicholson Head of Grid RenewableUK 07595 650 606, Tim Russell, the REA's Electricity Transmission and Distribution expert, on 07715 119 841 or Graham Meeks, Director, 020 7828 4077.

Yours sincerely,

By Email

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Association of Electricity Producers

Guy Nicholson
Head of Grid

Gaynor Hartnell
Chief Executive
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Graham Meeks
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Appendix 3

Our 5th July 2010 Submission

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Rachel Fletcher
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5th July 2010

Dear Rachel,

Changes to EHV charging methodology for pre 2005 Distribution Connected Generation – Interim Arrangements

The Association of Electricity Producers (AEP) represents large, medium and small companies accounting for more than 95 per cent of the UK generating capacity, together with a number of businesses that provide equipment and services to the generating industry. Between them, the members embrace all of the generating technologies used commercially in the UK, from coal, gas and

nuclear power, to a wide range of renewable sources of energy. RenewableUK (formerly the British Wind Energy Association (BWEA)) is the trade and professional body for the UK wind and marine renewables industries. Formed in 1978, and with 601 corporate members, RenewableUK is the leading renewable energy trade association in the UK, representing the large majority of the UK's wind, wave, and tidal energy companies. The REA is the industry association representing renewable energy producers. It is the largest renewable energy trade association in the UK and covers heat, transport fuels and biomethane injection as well as electricity generation.

We wrote to you in February 2010 outlining concerns we had regarding Western Power Distribution's proposals in respect of changes to its EHV charging methodology for pre 2005 Distribution Connected Generation. Since then a number of our membership participated in an Energy Networks Association workshop on this issue. We have now been notified that some Distribution Network Operators intend to introduce an interim EHV charging methodology for implementation in October 2010. This is prior to agreement on the enduring arrangements for pre 2005 Distribution Connected Generation to be introduced in April 2011 should there be evidence that change to the current arrangements can be enforced.

Our members have significant concerns regarding the introduction of GDUoS charges for all pre-2005 EHV connected generation, including the interim arrangements now emerging for application from October 2010. In our original consultation response we highlighted that the proposal and the principle of charging pre- 2005 EHV connected plant:

- failed to respect property rights held by generators that connected prior to April 2005 (and paid large fees including a capitalised O&M costs in lieu of ongoing charges);

- were not cost reflective and did not include adequate compensation provisions;

- were likely to lead to a material distortion in competition in the generation market, given the unequal treatment of pre-2005 generators from 1 April 2010;

- must undergo a full and detailed impact assessment recognising the implications of this proposal across the entire GB DNO network.

There is nothing in the most recent proposals which alleviate any of those concerns.

Pre-2005 connected generators Contractual Terms and Conditions

We have previously stated that we are opposed to the implementation of GDUoS charges on pre-2005 EHV connected generation and, in support of that view, explained that members had made their original siting decisions on future build viability by choosing to pay an up-front charge to reflect the use of the system rather than paying an annual charge. These large upfront costs were paid at the time of connection in the clear expectation that there would be no ongoing additional charges.

We were invited by the Energy Networks Association to enter into direct dialogue on this topic and members presented their views at the 6th May meeting. At this point we believed there to be three options on the table:

1. to implement Generator Distribution Use of System charges with a refund based on actual amounts paid

2. to refund based on future Generator Distribution Use of System charges expected until the end of all pre paid rights

3. or to defer payment until end of contractual rights.

Have investigations into each of the three options concluded? We believed that each is still being evaluated by the Distribution Network Operators and Ofgem.

Our expectation was that following publications of the cost benefit analysis behind each proposal, and further consultation, this may have led to implementation of charges (with compensation paid) from April 2011 or continuation of the status quo. However, it appears that Distribution Network Operators are being pressured into putting in place interim arrangements before April 2011. This is prior to any decision proving beyond doubt that the current contractual agreements can be amended and that there is a case for change. This would appear to be pre judging the outcome of the work to introduce enduring arrangements from April 2011.

Why not choose to defer any charge in the interim period, as this is one of the options supposedly under consideration? We see no value in introducing interim charges that will in all circumstances bear no resemblance to any enduring charges that may be introduced. This will have budgetary implications for all affected parties whether supply or demand. Of most concern however is the introduction of this retrospective change to the nature of access rights. By doing so in this manner, for no apparent reason, Ofgem is sending a signal to investors, which will undermine confidence of the stability of the GB market.

Cost Reflectivity

Some of our members have received indicative interim Generator Distribution Use of System charges for their stations and wish to raise concern regarding the level of some of the charges which appear to have been set at an extraordinarily high level and casts doubt upon how cost reflective the charges really are. Significant concerns were highlighted regarding cost reflectivity of WPD's proposed charges effective from April 2010. It appears those concerns have not been addressed and we would argue the interim charges are non-reflective and therefore cannot be implemented.

Distortion to competition

This issue was discussed in depth at the recent Distribution Charging Methodologies Forum. There appears to be substantial differences in the charging methodologies and payments that may be introduced from 1st October 2010. The charges being proposed by WPD are significantly higher than the charges being proposed by other Distribution Network Operators. We also understand that some Distribution Network Operators are not proposing to levy any charges from 1st October 2010. This is going to introduce a postcode lottery which will materially distort competition in the generation market.

We would also like you to note that the introduction of interim charges from 1 October 2010 will generate very different charges from the enduring regime from 1 April 2011. This will result in (further) regulatory uncertainty for pre-2005 connected generators. Presumably, there will also be an associated tariff disturbance for other users of the distribution networks, unless the allowable revenues of the distribution companies for this year are to be adjusted.

Compensation

Despite AEP members actively engaging in the Energy Networks Association workshops to discuss compensation no real progress appears to have been made. The introduction of charges and the issue of compensation are

inextricably linked and we do not believe charges can be implemented without addressing the issue of compensation. It is very unlikely compensation agreeable to the generator community will be agreed prior to 1 October 2010 and therefore we cannot see how interim charges can be implemented.

Impact assessment

We believe that the proposal to levy charges on pre-2005 generators across the network as a whole has not been properly assessed. Although the issue was discussed in the context of Distribution Price Control 5, the materiality of the changes has only come to light in recent months. While we now have better visibility of the costs of this proposal, we still have no understanding of the benefits to customers of such a change. We therefore reiterate, as a minimum, the need for a formal impact assessment to be undertaken.

Members preferred position is the maintenance of the current charging arrangements but if charges are to be implemented appropriate compensation must be paid to individual generators. We are not aware of any customers or generators that consider the current situation in any way discriminates against them.

Conclusion

We have fundamental concerns that Distribution Network Operators are introducing charges to pre-2005 EHV-connected generation in a hurried and inconsistent way. We believe that this could lead to unforeseen and potentially material distortions to the generation market. We also believe the implementation of the charges fundamentally ignores the property rights enjoyed by our members. We therefore believe that interim charges should not be implemented.

As a minimum, we would ask Ofgem to undertake an impact assessment on the proposed changes and the costs and benefits of the proposals.

Should you have any questions please contact Barbara Vest, Head of Electricity Trading Association of Electricity producers on 07736 197 020 or Guy Nicholson Head of Grid RenewableUK 07595 650 606 or Tim Russell, the REA's Electricity Transmission and Distribution expert, on 07715 119 841

Yours sincerely,

By Email

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Chief Executive
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Gaynor Hartnell
Chief Executive
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Appendix 4

Our 11th February 2010 Submission

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Ofgem
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11th February 2010

Dear Rachel,

Consultation on Western Power Distribution's (WPD) modification proposal 016 to introduce changes to its EHV charging methodology

Thank you for giving us the opportunity to comment on this important consultation. This response has been developed from within the AEP membership and is supported by the British Wind Energy Association. The Association of Electricity Producers (AEP) represents large, medium and small companies accounting for more than 95 per cent of the UK generating capacity, together with a number of businesses that provide equipment and services to the generating industry. Between them, the members embrace all of the generating technologies used commercially in the UK, from coal, gas and nuclear power, to a wide range of renewable sources of energy.

We have significant concerns over WPD's proposal and the AEP also has more general concerns regarding the introduction of GDUoS charges for all pre-2005 EHV connected generation.

In particular, we believe that the proposal and the principle of charging pre- 2005 EHV connected plant:

- fails to respect property rights held by generators that connected prior to April 2005 (and paid large fees including a capitalised O&M costs in lieu of ongoing charges);
- is not cost reflective and does not include adequate compensation provisions;
- is likely to lead to a material distortion in competition in the generation market, given the unequal treatment of pre-2005 generators from 1 April 2010 that is emerging across DNOs and an enduring distortion between transmission and distribution connected generators;
- should, as a minimum, be subject to a full and detailed impact assessment (recognising the implications of this proposal not just to connectees in WPD's region, but across the entire GB DNO network).

Pre-2005 connected generators

We are opposed to the implementation of GDUoS charges on pre-2005 EHV connected generation. AEP members made specific siting decisions on future build viability by choosing to pay an up-front charge to reflect the use of the system rather than paying an annual charge. These large upfront costs were paid at time of connection in the clear expectation that there would be no ongoing additional charges. As recently as September 2009, WPD acknowledged as much, setting out in its response to Ofgem's Initial Proposals for DPCR5 that:

"…the expectation at the time most pre-2005 generators connected was that they would never pay GDUoS charges[2]..."

The AEP has concerns regarding the robustness of the proposed methodology for pre-2005 generators. The connections were designed and sized for the connecting generator with very limited spare capacity. Therefore even small increments of growth are likely to trigger reinforcement which is likely to create significant volatility and produce large non cost reflective charges.

In its proposed methodology WPD has proposed addressing the upfront charges that were paid (in part) through specific adaptations to its methodology (most notably by removing assets most clearly associated with pre-2005 generators). However, this is inadequate given the expectation that all costs incurred by

[2] See page 22 of Part 3 of WPD's response to Ofgem's DPCR5 Initial Proposals document, on the Ofgem website.

networks in allowing pre-2005 generators to export power onto the network were included in the initial upfront charge (including capitalised O&M charges).

The AEP does not believe this amendment provides an adequate level of recompense. The only way to adequately reflect the property rights enjoyed is to ensure compensation is comparable to the prevailing GDUoS charge. As a minimum the charge should reflect the amount that generators have overpaid under the current deep charging regime by paying for a number of years' access up front which subsequently has not been fully delivered. We note that the WPD proposal does not even refund in all cases the full contribution of upfront connection costs as explained in footnote 17 of the consultation.

We believe that, if accepted, WPD's proposal would set a damaging precedent, significantly increasing the level of regulatory risk in the GB market. This could have serious implications – particularly at a time when security of supply concerns are becoming increasingly important and investment in new plant will be required.

Distortion to competition

It is clear that the level of charges being proposed by WPD is highly material. We also understand that charges are being proposed by other DNOs for pre-2005 EHV-connected generation from 1 April 2010, but that the methodologies being applied by these DNOs vary significantly.

Setting aside the issue of the legality of the proposed charges, it is unclear whether the unequal treatment of pre-2005 generation from 1 April 2010 is driven by underlying differences in the costs these plant impose on the networks to which they are connected, or whether these are spurious differences resulting from inconsistent choice of methodologies. If the latter, then there is a strong likelihood that the generation market will face a material distortion.

The AEP would also like you to note that the introduction of interim charges from 1 April 2010 and potentially very different charges based on an enduring regime from 1 April 2011 will result in (further) regulatory uncertainty for pre-2005 connected generators.

Impact assessment

We believe that the proposal to levy charges on pre-2005 generators – not just in the context of WPD's proposal, but across the network as a whole – has not been properly assessed. Although the issue was discussed in the context of DPCR5, the materiality of the changes has only come to light in recent months. While we now have better visibility of the costs of this proposal, we still have no understanding of the benefits to customers of such a change.

Conclusion

We have fundamental concerns that DNOs are introducing charges to pre-2005 EHV-connected generation in a hurried and inconsistent way. We believe that this could lead to unforeseen and potentially material distortions to the generation market.

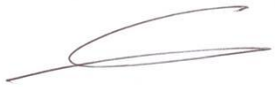
We also believe the implementation of the charges fundamentally ignores the property rights enjoyed by AEP members. Therefore we suggest that Ofgem vetoes WPD's proposal, and extends the current exemption to allow industry to more thoroughly consult on the proposal to apply charges to pre-2005 generation as part of the ENA's consultation process.

As a minimum, we would ask Ofgem to undertake an impact assessment on the changes proposed by WPD, and subsequent proposals as they emerge to understand in more detail – and have the opportunity to comment on – the costs and benefits of the proposal. In particular, we believe that other large embedded generation units face similar issues to those faced in WPD's region, and so the issue requires wider consideration. We would be happy to work with Ofgem to develop a more robust and enduring methodology.

Please let me know if you would like to discuss any of these comments further.

Yours sincerely,

By email



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