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Distribution Policy
Ofgem
9 Millbank
London
SW1P 3GE

07 July 2011

Your ref: 67/11

Our ref: Oncons/10/10053

Sent by email only to Ynon.Gablinger@ofgem.gov.uk

Dear Ynon,

ELECTRICITY DISTRIBUTION CHARGING METHODOLOGIES: DNOs' PROPOSALS FOR HIGHER VOLTAGES

Thank you for the opportunity to respond to the above consultation of 20th May 2011 and we are grateful for your flexibility in submitting our response. I am pleased to submit this response on behalf of ScottishPower Renewables (SPR).

As the UK's leading developer and operator of wind generation projects, we have considerable experience of working within the current arrangements for distributed generation. Onshore wind remains a key element of achieving the Government's energy policy objectives in respect of moving to a low carbon, secure electricity market. With much of onshore wind – and other forms of low carbon generation - being connected to distribution networks it is therefore vitally important that these arrangements support the growth in embedded generation that will be required to achieve these policy objectives. Please note that we have restricted our comments on the consultation to charges for generators.

EDCM principles and objectives

The objectives for the proposed EHV Distribution Charging Methodology (EDCM) are strongly based on cost reflectivity, to signal the cost to users of using the network at their particular point of connection. Thus users connecting in areas of low demand and/or low network capacity are likely to face higher charges than those connecting in other areas. Much of the existing and potential onshore wind sites are located in remote areas of low demand but where the wind resource is at its greatest. Therefore a move to greater cost reflectivity in distribution charging is unlikely to maximise deployment of onshore wind or to support achievement of the Government's wider energy policy objectives.

By providing strong locational signals, EDCM also aims to encourage customers to locate where there is spare capacity. However, the high number of projects wishing to connect to the distribution network makes this charging signal potentially very changeable and unpredictable for generators and so such a signal may not be sufficiently stable and predictable to encourage and maintain investor confidence. Accordingly, we suggest that measures should be put in place to mitigate volatility in charges thus ensuring tariffs and charges are more predictable.

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In addition, in the absence of published tariff charges, generators will not be able to identify the strength of cost signal they may face, without having to ask the DNO for indicative charges. As well as imposing a resource burden on the DNOs, this is unlikely to be sufficiently flexible for generators to be able to optimise their projects' location and/or operating plans. We believe that this lack of transparency in setting charges undermines the principles of tariffs being transparent etc.

It is important that the methodology is not only stable and predictable but also that it is enduring. To achieve the policy targets, high levels of embedded projects will connect in the coming years, and so the model must accommodate that without requiring significant or fundamental change in the short term.

We consider that there is still a high level of uncertainty around the EDCM arrangements and that insufficient time has been allowed for users to understand and incorporate the impact of such changes into business plans and budgets etc. For example, the level of final charges has only been known recently and some have changed considerably since the last indicative tariffs issued in January 2011. Additionally the levels of refunds to those sites that were connected prior to 1st April 2005 (pre-2005 generators) will not be agreed by the DNOs until after the proposed EDCM implementation date. In addition, we believe that the case for charging pre-2005 generators for DUoS has not been thoroughly justified yet. All of these factors undermine confidence in the arrangements and so present risk to investors.

Pre-2005 connected generators

The consultation states that pre-2005 generators should be charged for UoS on the same basis as post-2005 generators in order that there is no undue discrimination between generators and that all DG are encouraged to connect to and use efficiently DNOs' networks. In common with other industry members, as far as we are aware, no post-2005 generator has made any representation to Ofgem that they are being unfairly discriminated against on this basis. Therefore, such an arrangement would seem not only to be unnecessary, but undermines confidence in the stability and predictability of the regulatory regime.

The introduction of DUoS charging for pre-2005 generators will have a significant impact on the financial viability of some projects. Of our embedded portfolio, some 65% by capacity connected pre-2005 and so we are particularly keen to ensure that pre-2005 generators are treated fairly and appropriately. Consequently, we consider that parties who connected to a distribution network prior to April 2005 (under a regime where generators connecting to a distribution network paid deep connection charges but no UoS charges) should be able to maintain that position. At the very least, they should be fully compensated for any double charging of O&M costs, additional costs and the change in their contractual position.

At present there is no firm definition of the basis of the refunds to be made by the DNOs to pre-2005 generators or how they are to be calculated. The consultation states that guidance on this will be published in the summer of 2011 and we would therefore expect the situation to become clearer in the coming months. However, in order to conclude this, all affected parties will need to gather and analyse historic contractual information and evidence relating to the value and the components of the connection charges for these pre-2005 DG generation sites, many of which connected well before 2005. It will be a challenge to conclude this definitively before April 2012, which is clearly some months after users are being asked to confirm their support for the EDCM principles and methodology.

It is also important to note that given the passage of time, the parties may not be able to locate all of the information necessary to establish the basis or extent of the components of

their connection charge in each case, including the value of any O&M component which was included and which now may be subject to double charging under EDCM. Clear guidance must be given on how to deal with such situations along with guidance on how any disputes regarding refunds will be resolved.

In these circumstances, SPR considers that the timetable proposed for the introduction of EDCM is inappropriate and unrealistic.

Implications of interaction with other ongoing industry changes

Due to the different nature of the networks, the consultation states that Project TransmiT (Ofgem's review of transmission charging) will not necessarily have implications for the distribution charging methodology, and if there are implications Ofgem may seek to incorporate them, through the open governance processes to which the distribution charging methodologies will be subject, or by conducting a significant code review of the existing distribution charging code.

We are concerned about this approach for a number of reasons. Firstly, for many of the reasons described in this letter regarding deployment of onshore wind, Project TransmiT could conclude that changes are required that lessen the cost reflective signals to users, in order to achieve wider Government energy targets. It seems appropriate to us that there should be consistency between models and methodologies used to set charges for use of networks and that the EDCM proposals (including in respect of implementation) should be kept under review pending the outcome of TransmiT.

In addition, Ofgem's proposed 'wait and see' approach to the outcome of Project TransmiT provides a high degree of uncertainty for existing and new users, that undermines investor confidence and so could lead to projects being at best delayed or at worse cancelled.

In addition, we believe that implementing such a significantly new approach to DUoS charging while EMR is underway should be reconsidered. The EMR could have significant implications for embedded onshore wind projects and so this should be considered alongside any changes to charging methodologies.

Further, in common with other energy policy initiatives, we believe that greater consideration should be given to consistency with EU approaches to charging in order that UK generators are not disadvantaged as an integrated European energy market develops.

EDCM impact

The consultation states that for around 20 per cent of the customers, the new methodology will see potentially large increases in their charges and that after the proposed implementation in April 2012, there may also be some volatility in charges due to the assumptions and calculations used in the methodology. By the application of EDCM to all of our embedded generation portfolio SPR will experience an overall increase of around 95% in our distribution UoS charges, including an increase in excess of 600% in our export UoS charges. We believe that such an increase in charges cannot be justified and applying them at such short notice is also unjustified.

The consultation considers that DNOs should develop a package of measures to help customers manage their charges. We agree with and support this initiative, but to date the DNOs do not seem to have issued any information on this. Consequently, we believe it is unlikely that customers will have sufficient time to develop and implement any appropriate changes to their behaviour before EDCM implementation.

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We believe that the main benefits of such guidance will be realised if the implementation of EDCM is delayed. By that time, customers will have had more time to consider, understand, respond to and allow for the implications of the proposed methodology.

Credits for Intermittent Generation

SPR welcomes Ofgem's proposed conditions on EDCM and in particular the credits for intermittent generation. At present credits are only available for non intermittent generation. This would appear to be discriminatory against intermittent generation which can also provide some benefits to the system in terms of reducing reinforcement costs.

EDCM implementation date

SPR considers that it is important to implement a methodology that is robust, fair, transparent and stable even if this means the proposed implementation date has to be delayed. Therefore we believe that the proposed implementation date of April 2012 should be delayed and we support a later implementation date that would allow the uncertainties and impacts to be fully considered and addressed, including the implications of the conditions that Ofgem suggest DNOs may have to incorporate. We believe that an implementation date of April 2013 is more realistic on the grounds that:

a. The level of final charges has only become known recently having changed considerably since the last indicative tariffs issued in January 2011. We believe that insufficient time has been allowed for generators to factor these charges in to project models, budgets and business plans.

b. The case for charging pre-2005 generators for DUoS has not been thoroughly justified.

c. The refunds to pre-2005 generators have not yet been agreed with generators and it will be challenging for them to be agreed before the proposed EDCM implementation date of April 2012. It seems unreasonable to expect generators to support the implementation of a methodology which significantly weakens their cost base and contractual position before they know the level of refund they will receive.

d. The implications of the outcomes of Project TransmiT, EMR and EU requirements should be considered prior to implementing a new methodology

With regard to the specific questions raised in the consultation, where we have views but we have not addressed them above, our responses are given below:

Q 4.1 Do you agree with our proposal to modify the generation revenue target in order to avoid double charging for operations and maintenance costs on sole use assets? This issue aside, do you agree with our view that the approach to calculating a generation revenue target is reasonable? &

Q 4.2 Do you agree with our assessment that the approach to scaling is reasonable?

We agree that double charging should be avoided. With regard to scaling, we do not see how this is consistent with the aim for cost reflectivity and therefore we question whether it is appropriate.

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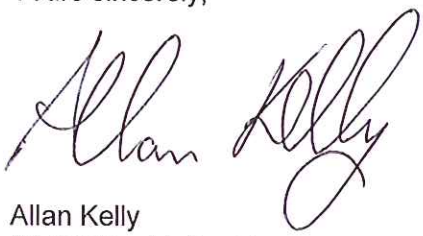
We hope you find our comments clear and helpful but we would be happy to discuss them more fully with you. If you would like to do so, please contact me on 0141 568 4748 or at allan.kelly@scottishpower.com.

Yours sincerely,



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