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Dear Geoffrey,

RE: Review of NGET Licence Condition C13

This letter addresses the issues highlighted in our recent discussion on 10 January 2012 about the advantages of reviewing the expiry of the small generator discount, as set out in Licence Condition C13. The link between the small generator discount and prevailing charging arrangements for embedded generators was established as part of the DECC / Ofgem consultation at the introduction of BETTA¹. In this letter we present a possible timetable for the progression of enduring embedded generation charging arrangements whilst taking account of progress on other fundamental changes, principally those under the umbrella of Project TransmiT.

In principle we are seeking to avoid parallel development of the enduring locational Transmission Network Use of System (TNUoS) charging arrangements, which are expected to be directed under Project TransmiT, and fundamental changes to the enduring charging arrangements for embedded generation. The main reasons for this were covered in our letter of 24 December 2011.

Following on from this previous correspondence, we recommend that the provisions of Licence Condition C13 are extended to **April 2016**. This provides regulatory certainty to all affected parties, whilst balancing the need to progress this issue in a timely and inclusive manner and minimising the potential for the need for further changes to C13. This is explained in greater detail, below.

Consultation process

In our previous discussion we highlighted our concern that the main parties likely to be materially impacted by any proposed change to embedded charging arrangements in England and Wales would be sub 100MW distribution connected generation. These parties are not normally signatories to the CUSC or have a direct relationship with NGET. Indeed NGET's visibility of these is mainly through Grid Code obligations on Distribution Network Operators. As part of our discussion we initially suggested that you may wish to consider this as an area for a Significant Code Review

¹ Small Generator issues under BETTA, November 2003

(SCR). However, as a result of the issues discussed, we now recognise the limitation of the SCR approach in addressing this issue and agree that NGET would be best placed to lead the Industry debate.

In progressing this issue, we believe that we would need to broaden the normal CUSC process to ensure any proposals that are presented to Ofgem have been adequately consulted upon by all materially affected parties. Whilst we would need to discuss process with the CUSC Panel, we believe that it would be necessary to engage with the DCUSC Panel and possibly have extended consultation periods in order to facilitate effective engagement with all relevant stakeholders.

Interaction of timelines

The current timeline for the TransmiT CUSC process is that it will be initiated in April 2012, with a CUSC report likely to be submitted to Ofgem in October 2012. This timeline would allow for a decision to be made in early Spring 2013 and the potential for implementation of a new TNUoS charging regime in April 2013. The key issue for interaction with an embedded generation charging proposal is the need for a stable baseline against which proposals can be quantified, assessed and codified (i.e. legal drafting). Therefore if actual implementation, as opposed to the decision, was delayed this should not immediately impinge on the proposed timeline (i.e. our proposed timeline is not directly reliant on TransmiT implementation).

We note a possible interaction with any change to the 'G/D' split that may arise either directly out of TransmiT, or possibly through the development of the EU Tariff Harmonisation Guidelines. Should it be decided that demand Users ('D') should fund an increased proportion of overall transmission revenue, such proposals may seek to change the charging base for demand. This could have a crossover with our proposals for addressing embedded benefits through gross charging of demand. For example, if we were to define demand excluding embedded generation this would remove the embedded benefit (for TNUoS).

We are also mindful that responses to TransmiT have suggested that an April 2014 would be a more appropriate implementation date. This view mainly reflects parties' concerns over the potentially inefficient windfall gains and losses that a change to charging arrangements can create if they are implemented after the annual contracting rounds (in this case April 2012 and October 2012). As a result of the magnitude of potential impacts, the complex nature of proposed changes, any necessary quantitative assessment of proposals, and any subsequent Ofgem impact assessment, an implementation after April 2013 is increasingly likely. In addition to this the CUSC process and the Ofgem assessment should not be unduly fettered by a deadline in relation to C13, and that a further change to C13 creates continued uncertainty for market participants.

As well as the CUSC change, in order to implement National Grid's preferred model we estimate that we would need to raise a BSC modification proposal in June 2012 (to replicate the effect of the rejected P260 proposal). We also expect a number of alternatives to any CUSC proposal and it is likely that these will also have associated BSC and possibly DCUSC consequential changes. As these will be raised during the CUSC process this would also frustrate the robust assessment of all the proposals prior to April 2013.

Proposed timetable

From the above, and based on a TransmiT decision before April 2013, we would propose the following timetable:

- Raise an embedded generation CUSC modification proposal in April 2013
- CUSC working group process and any consequential changes raised April 2013 to December 2013
- Ofgem decision April 2014
- Transition period April 2014 to April 2016

To facilitate this process we would recommend that C13 is extended to **April 2016**, with the ability for it to be withdrawn if any revised arrangements are implemented prior to April 2016. This timeline recognises the need to have a robust and broad industry consultation and seeks to best remove uncertainty from market participants.

Next steps

It is important that we remove any uncertainty on the future of C13 and also future development of embedded changing arrangements. We would suggest the next steps could be either proceeding straight to a licence change or noting the interaction in the TransmiT SCR conclusions and indicating that a licence change will be progressed later in 2012, both approaches would go some way towards removing uncertainty.

We would be interested in your thoughts on this proposal and next steps. If you have any queries on the issues raised please contact myself or Ivo Spreeuwenberg.

Yours sincerely,

Patrick Hynes

By email only