

28 June 2013

Ben Smithers
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Dear Ben

Response to Ofgem Consultation: *Creating the right environment for demand-side response*

BUUK is the parent company of distribution licensees The Electricity Network Company Limited and Independent Power Networks Limited. Both licensees are commonly referred to as IDNOs and differ from DNOs in that they own and operate '*last-mile*' networks and are subject to relative price control arrangements.

Our response is limited to how an environment for demand side response will be inclusive of IDNOs. Although the consultation discusses the potential benefits and incentives to DNOs, it does not describe how these could feed through to IDNOs. IDNO networks will provide aggregated "chunks" of demand which connect to DNO networks at disparate locations across DNO groups. If demand-side response is to become an attractive proposition for IDNOs then it needs to offer the equivalent incentive mechanisms available to DNOs and industry frameworks where customers on IDNO networks can participate in such arrangements.

Above all we need to ensure that demand- response mechanisms neither distort nor prevent competition. Our response to Ofgem's questions is provided in the appendix to this letter.

We would be happy, through industry workgroups or otherwise, to engage with Ofgem to develop appropriate arrangements for demand-side response.

Yours sincerely

Mike Harding
Head of Regulation

Appendix 1 Response to Ofgem Questions

Precondition 1

Question 1: *Are there any additional key challenges associated with revealing the value of demand-side response across the system? If so, please identify and explain these challenges.*

As Ofgem recognises, the requirements for demand side response will differ between industry participants in the supply chain. The need to move or reduce demand on a distribution system or part of a distribution network may not be coincident with the need to move or reduce demand on a transmission system or the need for suppliers or generators. Therefore, there will inevitably need to be some form of 'balanced' trade off between parties in the supply chain to ensure that incentives or benefits from one part of the supply chain do not cause perverse consequences on other parties.

Question 2: *Can current regulatory and commercial arrangements provide the means to secure demand-side response being delivered? If not, what will regulatory and commercial arrangements need to deliver in future?*

If customers invest in demand response measures how will their return on the investment be guaranteed. This needs to be considered in providing connections as well as through charges for use of system.

For customers deemed to be connected at EHV network tiers, charges for use of system are subject to the EDCM. One of the issues with the EDCM is that an existing customer may be penalised (through higher or lower charges) for actions taken by other customers (either by connecting new premises or increasing demand at existing premises or by moving away), irrespective of what actions a customer may take in respect of demand-side response measures. It would therefore appear necessary to amend the charging methodology so that the benefits a customer receives by implementing demand side measures are protected for a specific period. This may be longer than a price control period depending on the nature of investment.

The actions of one customer to reduce demand (and thereby increase capacity headroom on the network) can be thwarted if another customer takes up the capacity. Therefore the customer has no certainty that they will be able to recover their investment in demand side management over the longer term. In establishing demand-side response arrangements some certainty needs to be in place as to whether the arrangements reside with the occupier or with the premises. If the arrangements reside with the occupier then demand-side response arrangements fall away on a change of occupier. This would create uncertainty for a distributor in respect of making system investment.

We would also like to understand how demand-side response arrangements fit with the provisions of sections 16 to 21 of the Electricity Act 1989. Under Section 16 of the Act a distributor is required to make a connection where it is requested to do so, and section 16(4) makes it clear that making a connection includes maintaining a connection. Maintaining a connection, we presume, includes maintaining the maximum power requirement. However, connections with demand-side response arrangements could be considered as falling under section 22 of the Act and therefore outside the remit of Ofgem for dispute determination.

Question 3: *Is current work on improving clarity around interactions between industry parties sufficient? If not, what further work is needed to provide this clarity?*

We note the useful work undertaken through Work Stream 6 of the Smart Grids Forum. This recognises that demand-response mechanisms may be more complicated where ICPs and IDNOs are involved. We agree that whatever mechanisms are put in place they should not distort nor prevent competition.

We would be happy to engage with relevant parties to assist in the development of solutions in this respect.

Precondition 2

Question 4: *Are there any additional key challenges associated with effectively signalling the value of demand-side response to consumers? If so, please identify and explain these challenges.*

At present a significant barrier to the development and implementation of more granular tariffs is the ability to implement them through existing metering stock. However, the roll out of smart metering will remove this barrier. It is therefore possible that more granular tariffs (i.e. tariffs with a greater number of time pattern regimes) could be developed to record electricity at different times of day and or on a seasonal basis. Additionally tariffs could be more locational to recognise different demand hot spots. The only way of doing this at present is through making line loss factor class codes locational. At present the LLFC is a numeric 3 digit code. To facilitate greater locational granularity the number of LLFC combinations needs to be increased significantly. This change potentially impacts significantly on the systems of all market participants. Nonetheless, such an approach would enable consumption patterns to be more tightly grouped on a geographic basis and facilitate the development of more granular localised tariffs. It is accepted that this would add a degree of complexity to the CDCM.

We note that Section 3A of the Electricity Act places a duty on the Secretary of State and the Authority to have due regard to the interests of individuals residing in rural areas. Care would need to be taken to ensure that such measures were not in conflict with this duty.

Question 5: *Do you agree that signals to customers need to improve in order for customers to realise the full value of demand-side response? Does improving these signals require incremental adaptation of current arrangements, or a new set of arrangements?*

We agree that signals to customers need to be clear and that in the shorter term (say 5 to 10 years) this could be achieved through adaption of current arrangements. In the future there may be scope for new arrangements. However, at the present time we have difficulty in assessing what the likely value that will realistically be realised from implementing demand-side response. This needs to be gauged against the cost of developing any systems.

In developing demand-side response arrangements it is the ease with which customers can use them which will determine the extent that they are taken up. Work needs to be undertaken to assess what the size of the benefit compared to the constraints makes it worthwhile for them to engage in demand-side response.

Question 6: *To what extent can current or new arrangements better accommodate cross-party impacts resulting from the use of demand-side response?*

Not answered.

Precondition 3

Question 7: *Are there any additional key challenges associated with customer awareness and access to opportunities around demand-side response? If so please identify and explain these challenges.*

There has been significant public awareness of competition in supply since its introduction in 1998 yet there still remains inertia for people to switch, even though it has been in place for 15 years.

There are many reasons for such inertia; however, there one area may be around public confidence and trust in the market to do the right thing for the customer. Building confidence and trust in the new products is one of the significant challenges.

Question 8: *Is any additional work needed to explore the role of third parties in helping customers to access and assess demand-side response offerings?*

Not answered.

Conclusion

Question 9: *Are there additional preconditions for delivering the right environment for demand-side response? If so, please explain what these are and why they are important, as well as attaching a priority relative to those challenges we have already identified.*

Not Answered

Question 10: *Do you agree with the priority and timing we have attached to addressing each of the key challenges identified above?*

Not answered.