Distribution generators,
consumer groups and other
interested parties

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Date: 1 September 2014

Dear colleagues,

Views on security arrangements for liabilities arising in respect of works to the transmission system required to connect distributed generators

Users of the transmission system are required to underwrite works to the transmission network that are needed to connect them to the electricity network. They face a liability in the event they terminate their project, and are required to place security with National Grid Electricity Transmission plc (NGET) in respect of this. These are known as the user commitment arrangements. A Connection and Use of System Code (CUSC) Modification (CMP223) has been raised to change the arrangements for generators who are connected to the distribution network, but where works would also be required to the transmission system in order for that generator to be connected.

The CUSC working group has considered the changes and passed CMP223 to us to decide whether one of the options for change should be implemented. In order for us to reach a decision, we consider that further evidence is required. We have therefore asked distribution network operators (DNOs) for some additional data. A copy of the information request can be found on our website alongside this letter. At the same time, we would like to gauge the views of other parties, particularly embedded generators, who will be amongst those most affected by the proposal.

This open letter summarises the issues and the areas where we are seeking further information. We invite all interested parties, in particular embedded generators, to respond to the questions set out in this document by 3 October 2014.

Background

CMP223 was put forward by Carnedd Wen Wind Farm Limited in September 2013. They suggested that distributed generators may face undue discrimination because of the way that user commitment liability and security conditions are set out, and how the sums calculated are passed on by DNOs. Users connected directly to the transmission network post security at a reducing rate as the project nears completion – 42 per cent before key consents are granted and 10 per cent once these are achieved. Where works are required to the transmission network to connect a distributed generator, the DNO will arrange these works with NGET on behalf of the generator, and NGET will apply the user commitment arrangements to the DNO. The DNO will then pass this liability to the distributed generator. However, it may require the distributed generator to provide security equal to 100 per cent of the liability. This is because, unlike transmission operators, DNOs cannot recover any liabilities in excess of the amount of security from Transmission Network Use of System (TNUoS) charges in the event a distributed generator terminates its project.

The proposer suggested that requiring higher securities from generators that are connected to the distribution system than from those connected directly to the transmission system makes it harder for distributed generation to enter the market. Given that a study estimates that over

50 per cent of distributed generation is from renewable sources,[1] this could reduce the viability of new renewable generation projects, and so the ability of the UK to reduce carbon emissions and promote a low-carbon economy.

A summary of the proposals put forward under CMP223 to remedy this defect is set out in Annex 1 to this letter.

Issues

Security arrangements

CMP223 proposes changing the levels of security that would apply to a DNO in respect of the liability for works to the transmission system triggered by a distributed generator. The intention is that this level of security can then be passed down by the DNO to the distributed generator. Calculating and proposing suitable security requirements has proven difficult given the lack of access to information on distributed generation. To obtain a baseline, NGET undertook analysis of 31 larger distributed generators with whom it already has a contractual relationship (known as BEGA[2] and BELLA[3] generators) that either terminated or failed to pay any outstanding dues. Based on when the project terminated, the analysis suggested that the security percentages that should apply are: 45 per cent of the liability at the pre-consent stage as security, and 26 per cent at the post-consent stage.

The original and the alternative proposals developed by the workgroup (workgroup alternative CUSC modifications, "WACMs") all impose a new security requirement of 45 per cent (pre-consent) and 26 per cent (post-consent). They also require DNOs to provide annual figures to NGET on the termination rates of relevant distributed generation.

We have questions about whether the proposed security figures appropriately reflect the likelihood of a distributed generator terminating. First, the data used to generate these figures is not representative of all relevant distributed generators. Second, it may not take into account other factors that affect the risk or credit-worthiness of distributed generators compared to transmission-connected generators. Therefore the proposed security figures may not accurately reflect the risk to consumers. The information request issued to DNOs seeks further information to help us to understand whether the percentage proposed is appropriate.

Recovery of shortfall from TNUoS

The proposals for change all result in the shortfall between the user commitment liability and the security recovered from a distributed generator being ultimately recovered through TNUoS charges. The aim of this is to prevent the DNO facing a shortfall in the event that a distributed generator terminates a project. This should enable the DNO to mirror the security arrangements it has with NGET to the distributed generator.

The proposals put forward vary in the way in which this happens. In some of the options, NGET would be responsible for initially trying to recover the shortfall from a distributed generator, in other options this responsibility sits with the DNO. In our view, in order to be effective in remedying the defect any option would need to give the DNO sufficient certainty that the shortfall could be passed to NGET for recovery via TNUoS charges in a timely fashion. The option should also avoid imposing any unnecessary additional costs on any party.

We welcome views from stakeholders on whether the arrangements proposed achieve this.

[1] http://www.eti.co.uk/wp-content/uploads/2014/03/CarbonConnect_DistributedGeneration_PDF.pdf
[2] Bilateral Embedded Generation Agreement. This is an agreement between developers of large power stations and NGET. For more information on BEGAs, see http://www.ppaenergy.co.uk/web-resources/resources/e28a57c7978.pdf
[3] Bilateral Embedded Licence Exemptible Large Power Station Agreement. Applies to large power stations that are exempt from holding a generation licence; is only available to large power stations in Scotland. For more information on BELLAs, see http://www.ppaenergy.co.uk/web-resources/resources/e28a57c7978.pdf

Solutions outside the CUSC

As the arrangements between a DNO and a distributed generator are outside the scope of the CUSC, some stakeholders, as part of the workgroup process, suggested that a solution outside the CUSC could be more suitable to address the defect. One proposal suggested inserting an additional clause into the Construction Agreement to encourage DNOs to pass on the same security payment profile to relevant distributed generators that it received from NGET. However, there are two drawbacks to such an approach. First, NGET may not be able to legally impose such criteria on the DNO. Second, even if this results in DNOs passing on lower security requirements, the DNO has no provision for recovery in the Electricity Distribution Licence. Therefore, the solution does not address the shortfall between security provided and liability upon termination in the event of non-payment.

A modification to the DNO licence was also proposed to allow it to recover bad debt in a similar way that NGET can due to a special licence condition. However, in this scenario, the workgroup questioned whether customers of a particular DNO should underwrite assets that are part of the wider transmission system. Changes to Distribution Connection and Use of System Agreement (DCUSA) were also suggested to mandate DNOs passing on lower security arrangements. However, this suggestion was not further developed as it was outside the remit of the CUSC panel.

We welcome the views of our stakeholders on whether a solution outside the CUSC would be preferable, and what such a solution could be.

Our view

We have considered the evidence presented to us by the CUSC panel and the workgroup. While we have not reached any conclusions our initial view is that we would not be in favour of the original proposal, which requires relevant distributed generators to become signatories to the CUSC with the sole intention of benefiting from the section 15 arrangements. Becoming a signatory to the CUSC requires other commitments which could place a disproportionate burden on relevant distributed generators. Beyond this initial view, we think that more evidence is needed before we can make a firm decision on the merits of alternative proposals, including on the appropriateness of new proposed security levels.

Given the limited data behind the proposed new security requirements, we are requesting further information from DNOs and wider stakeholders. We would be grateful for your views on the questions set out below by 3 October 2014.

Questions

1. Do the proposals help reduce barriers to entry for smaller embedded generation projects?
2. Are the proposed security figures, of 45 per cent and 26 per cent (pre- and post-consent), representative enough of the risk of a relevant distributed generator terminating to be used as the basis for revised security requirements?
3. Is modifying the CUSC the best way to tackle this issue? Would solutions outside the CUSC better serve the requirements of relevant distributed generators?
4. Is a DCUSA modification necessary to ensure that DNOs apply these approaches consistently?
5. Should users with a BEGA or BELLA agreement have separate user commitment arrangements? Should the debt recovery process for these users differ from that of other relevant distributed generators given their contract with both National Grid and DNOs?

We welcome responses to this letter by 3 October 2014. Unless clearly marked as confidential, we will publish responses on our website. Please email responses to Saad Mustafa (saad.mustafa@ofgem.gov.uk).

Yours sincerely,

Catherine Williams
Head of Commercial Regulation, Electricity Transmission

Annex 1: The proposals

CMP223 proposes changing the user commitment arrangements for relevant distributed generators.

Full details of the modification can be found in the Final Modification Report.[4] The main elements of the original proposal, plus the alternatives are:

Issues	Original	WACM1	WACM2	WACM3	WACM4
Security required at 45% before consent and 26% after	✓	✓	✓	✓	✓
Debt recovery arrangements if the relevant distributed generator terminates without paying its full liability	Debt sits with National Grid, which attempts to recover it from the generator before seeking recovery through TNUoS charges	DNOs pay the full liability to National Grid. DNOs then attempt to recover debt before seeking reconciliation from National Grid. Debt sits with DNOs until we give approval to recover the shortfall through TNUoS charges	DNOs pay the secured amount to National Grid and attempt to recover the rest. Debt sits with National Grid until we give approval to recover the shortfall through TNUoS charges	DNOs pay the secured amount to National Grid for all relevant distributed generators (except BEGAs and BELLAs that have a direct contractual relationship with National Grid). Debt sits with National Grid until we give approval to recover the shortfall through TNUoS charges	DNOS pay the full liability to National Grid for all relevant distributed generators (except BEGAs and BELLAs that have a direct contractual relationship with National Grid). DNOs then attempt to recover debt before seeking reconciliation from National Grid. Debt sits with DNOs until we give approval to recover the shortfall through TNUoS

[4] http://www2.nationalgrid.com/UK/Industry-information/Electricity-codes/CUSC/Modifications/CMP223/

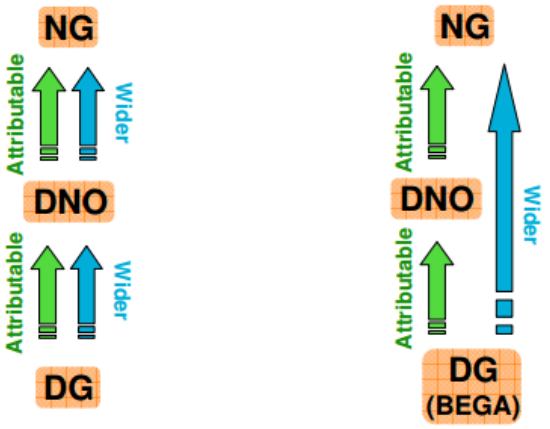
Treatment of BEGA and BELLA users	Mandatory changes. Introduces direct liability to National Grid for all liabilities for all relevant distributed generators	As now: BEGAs retain wider liability to National Grid. All other liability to DNO	As now: BEGAs retain wider liability to National Grid. All other liability to DNO	National Grid holds both attributable and wider liabilities	National Grid holds both attributable and wider liabilities
Post-commissioning liabilities	Not proposed, but there is scope for future introduction	As per existing arrangements	As per existing arrangements	As per existing arrangements	As per existing arrangements

The original and the WACMs all impose a new security requirement of 45 per cent (pre-consent) and 26 per cent (post-consent). They also require DNOs to provide annual figures to NGET on the termination rates of relevant distributed generation.

Differences between the proposals

The proposals differ across three areas:

1. Who recovers the debt and who accrues interest on it. The options diverge depending on the party that has the contractual relationship with the relevant distributed generator for the liability.
2. Security requirements for BEGA and BELLA users. Currently distributed generators (other than BEGA and BELLA users) must post security for attributable and wider works with the DNO, which passes it on to National Grid. BEGA and BELLA users post security for attributable works with the DNO, but have a direct contractual relationship with NGET for the wider liability, so they post security for that work with them. The diagram below illustrates the current arrangement:



These arrangements will change depending on the option taken forward. For instance, under WACM3 and WACM4 National Grid will hold both attributable and wider liabilities for BEGA and BELLA users.

3. Post-commissioning liabilities: While no option imposes post-commissioning liabilities on relevant distributed generators at the moment, the workgroup concluded that if the original proposal were adopted, there might be future scope to do so.