To : Donald Smith
Commercial Regulations : Electricity Transmission
Ofgem
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23rd December 2015

Dear Donald,

Response to consultation on the extension of the small generator discount

EDF Energy is one of the UK's largest energy companies with activities throughout the energy chain. Our interests include nuclear, coal and gas-fired electricity generation, renewables, and energy supply to end users. We have over five million electricity and gas customer accounts in the UK, including residential and business users.

We note that you propose extending further the Licence Condition 13 (LC13) discount, which has already been extended three times after its originally-programmed expiry date in 2008. It was designed to provide a level playing field for small 132kv-connected generators in Scotland only until industry developed enduring arrangements for transmission charging for embedded generators (EGs). The consultation document notes that the extension to 2019 is considered necessary because these arrangements have still not yet been developed as had been intended. This new proposal to further extend LC13, follows the rejection of CUSC Modification Proposal 239, which would have extended the discount (for up to 25 years) via the CUSC, in a discriminatory manner that only applied to existing qualifying generators.

EDF Energy does not support a further extension, as the sharp growth in the total amount of embedded generation this year, and its distortionary effects in the capacity market and more generally, mean that a full review and reform is now urgent. The matter should not be deferred any longer. We also note that this proposed extension of LC13 will create an adverse effect on the demand side as a class (and ultimately customers) of at least £15m a year, and growing into the future (via demand-side TNUoS charges). In addition this effect comes at very short notice, and is quite unexpected, as Ofgem made no hint, in its rejection of CUSC mod 239, to the effect that it was about to propose extending the actual LC13 discount (CUSC Mod 239 was only raised because no-one, including its proposer, expected any further extensions to the LC13 discount). Bringing in the change at such short notice is undesirable, leading to unexpected extra costs either for Suppliers, or, depending on the form of retail contract, their customers.

It has been our view for many years that fundamental reform to extend transmission charging to EGs needs to be developed – and that triad-based charging for demand is overdue for review. We do not view the very limited "net exporting GSPs" proposals from National Grid, which focus only on local charges for EGs, as amounting to such a reform at all. Local assets can serve both export and import functions- electricity can flow in either direction. The real issue, not addressed by Grid's recent proposals, is the cost of the impact of generation from EGs on the wider transmission network and its operation. TNUoS charges are calculated based on the impact of changes in generation on the wider transmission network – the cost of the incremental network investment that is needed. Grid's suggested local charges for "net exporting GSPs" do not take account of the cost of EGs using the wider transmission system – and do not give a cost-reflective locational signal. A change in the output of any EG, whether or not the GSP that it is connected to is exporting, will still have physical effects on (cause changes to) flows across the entire transmission system, and hence can contribute to, or defer the need for, transmission system investment. Therefore, the reform ought not to be focussed on exporting GSPs; the reform should more fundamentally consider the incremental impact that EG has on the need for transmission investment, and hence TNUoS charges.

We believe that it is important that work starts soon on developing arrangements for transmission charging for EGs, and believe that changes of such a scope and nature can best be taken forward via the *Significant Code Review* (SCR) process. The scope of the SCR should not be limited to TNUoS; a review is needed of the BSUoS charges to ensure that all parties using the transmission system, benefitting as they do from stable frequency, voltage and phase on an energised system, pay an appropriate share of those costs.

There is a strong case for also reviewing the current demand-side TNUoS charge-out basis. The long-standing "triad" basis assumes that only flows at times of winter peak demand are important in terms of transmission system investment. It has become apparent that with new patterns of flows and new types of generator connected to meet demand, it is not only generation/demand at time of winter peak demand that influence the need for transmission system investment, and this has been taken account of in the way generation TNUoS tariffs are to be calculated from 1 April 2016, thanks to Project "TransmiT". The exclusive focus on the times of winter peak demand in the application of demand-side TNUoS charging may no longer be appropriate. Related to this is the recovery of the residual charge element. As suggested by Frontier in their December 2015 paper on the distortionary effects of "embedded benefits" in the capacity auctions, consideration needs to be given to a "gross" charging approach which will help to address some of the embedded benefits distortion.

A critical reason that it is becoming impossible to continue to defer the matter of reforms to ensure that embedded generation bears its fair share of transmission and balancing costs, is to ensure a level playing field with transmission-connected generation in capacity auctions; the status quo is now causing a significant distortion, allowing a class of generator to compete more cheaply than if it faced its correct, cost-reflective transmission costs.

We are keen to discuss this matter further with you in the New Year but if you have any immediate questions regarding the issues raised in our response or have any queries, please contact Paul Mott on 0203 1262314.

I confirm that this letter may be published.

Yours sincerely,

Mark Cox
Head of Transmission & Trading Arrangements