

23<sup>rd</sup> September 2016

Frances Warburton  
The Office of Gas and Electricity Markets  
9 Millbank  
London  
SW1P 3GE

Anesco Limited,  
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Dear Frances,

**RE: OPEN LETTER – CHARGING ARRANGEMENTS FOR EMBEDDED GENERATION**

Anesco welcomes the opportunity to respond to Ofgem's Open Letter on charging arrangements for embedded generation.

Anesco is one of the UK's leading energy efficiency solutions companies. We were the first UK organisation able to bring together different technologies to deliver a customer's needs, while understanding Government incentive schemes, utility obligations and importantly tackling the bigger issue of climate change.

Focused on innovation and bringing the latest technologies and methods of best practice from across the globe, Anesco enables its customers to reduce their energy usage and save money, while reducing the world's carbon emissions. The company has forged strong relationships with manufacturers across the globe, including Europe, the US and Asia, working with a variety of teams and organisations to see how products and new innovations can be best developed and deployed for the UK energy market.

We welcome Ofgem's interest in understanding the role of network charging in ensuring consumers benefit from a lower-cost electricity network.

We are concerned that proposals to move to gross charging for embedded generators attempt to make the costs of using different networks comparable between different types of generators. A generator or demand user's position in the electricity market should reflect the costs and charges, including network charges, required to provide or receive their service.

It is not inherently wrong that differences in network costs between certain users should lead to competitive advantages in areas such as the Capacity Market. We are concerned that Ofgem is interested in equalising charges to improve the economics of specific market players.

We would reject Ofgem's comparison of network costs and the value of avoiding network costs with Capacity Market auction values. These comparisons incorrectly conflate the

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value of providing energy services with the value of avoiding network costs, which deliver two completely different services, and may or may not be of similar value depending on the circumstances.

If Ofgem decides that the triad TNUoS demand residual benefit for avoiding network use is not cost-reflective, then it should follow that the application of the TNUoS demand residual through the triad charge to network users is also not cost reflective.

By implementing changes only to the triad benefit Ofgem will not be directly addressing its identified non-cost reflective charge. We are unsure why Ofgem sees an 'urgent' need to address the consumer impact from an identified non-cost reflective charge on exported distributed generators, but has no urgency to address the impact of the TNUoS demand residual on half hourly metered customers.

It would be more appropriate for Ofgem to address the level of the triad charge caused by the fast-rising demand residual, rather than the benefit received by distributed generators.

We believe three steps would help address the fast-growing demand residual:

- Reduce the demand residual by reviewing the size of the money recovered from the locational charge, which is currently limited to just 10% of the overall costs of the network.
- Reduce the demand residual by reviewing whether there are specific network costs which should be socialised across all users.
- Review the triad signal and whether it is fit for purpose, including examining how it recovers both the residual, the year round and the peak charges.

We appreciate that Ofgem sees a need for a 'quick fix' focussed specifically on TNUoS demand residual triad benefit received by distributed generators. However, proposals to move to 'gross charging' for distributed generators, as proposed by CMP264, CMP265 and related alternatives, do not represent either quick or effective solutions.

We also appreciate Ofgem's concerns that a Significant Code Review carries risks of delays in implementing a solution. However, the need to move quickly should not mean Ofgem is obligated to use a solution which creates a range of new problems, especially when other alternatives – such as socialising the value of the demand residual – could more effectively address the growing TNUoS demand residual.

The concept of net charging, and subsequently the embedded benefit, has been a transmission network principle since the 1990s. The proposal to remove this principle and implement an entirely different charging regime in nine months is unrealistic and likely to result in significant harm to generators, suppliers, consumers and investors (both current and future).

The current proposals to charge distributed generators on gross require significant investments in suppliers' IT systems. The scale of these IT changes making it unlikely a move to gross charging can be implemented before 2019, and also making it likely that changes will result in significant cost increases to suppliers and these costs will eventually be born by consumers.

Ofgem would be better placed to look for more evolutionary changes which do not try to upend 20 years of charging principles, which would result in significant unintended results.

The regulator has required these modifications be placed on an 'accelerated' timetable. As a result of this timetable, the work group has neither sought, nor performed, nor reviewed, any new or existing analysis on the cost reflectivity of the embedded benefit. The work group was also not permitted to investigate the costs which are causing the TNUoS demand residual, or to understand how much of the demand residual should be classified as 'sunk costs'.

Ofgem has specifically tasked the work group to deliver its report to the CUSC Panel so the CUSC Panel can reach a decision by 28 November, which is 10 days before the Capacity Market and the latest date a CM participant can choose to exit. We do not think the work group will achieve Ofgem's requirement, as set out in the Open Letter, for "the benefits and costs" to be "properly assessed" and for these "to be considered during the modification process". Ofgem's required timetable has prevented the work group from properly assessing alternative options, requiring analysis of their impacts, or fully understanding the implications of their implementation.

We recognise Ofgem's concern that the TNUoS demand residual triad benefit is "distorting dispatch by dampening prices at peak times when EG dispatch out of merit to generate in the triad periods". Ofgem has also noted that distributed generators respond to a triad signal, and that this signal is unavailable to transmission connected generators "and hence is a distortion".

If Ofgem believes all generators should face the same charging mechanism and that this is a distortion, then we would suggest it would be more appropriate to reform the triad mechanism itself. For example, spreading the current triad charge over more periods would reduce distortions on dispatch. There would be especial merit in considering whether it is appropriate for the year round charge portion of the demand TNUoS to be based on delivery in peak periods.

However, Ofgem's focus on creating the same methodology for both distribution and transmission generation ignores the fact that distributed generators are not transmission network users. Instead, Ofgem should be aiming to find a charging mechanism which applies a single approach to both demand users and distributed generators, as these two types of users have the same impact on the transmission system and should receive the same signals.

We would also note that any changes to the triad mechanism methodology should be based on clear evidence reflecting the impacts of different network use on network costs. Additionally, any proposals should consider the different types of distributed generators and their different impacts on balancing costs, as intermittent distributed generators will have much different cost impacts than non-intermittent generators.

Finally, Investor confidence is essential to create the much needed motivation to deliver the future generation plant the UK requires. As the energy mix changes and historic fossil fuel based generation is closed down, ensuring a low carbon, efficient and reliable energy system can only be achieved with the appropriate level of private investment. Following

several years of change and reduction in incentives, further increase to the risks of investment in the UK energy market can only be counterproductive.

We trust that this feedback is useful and would welcome the opportunity to discuss Ofgem's plans further.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'Neil Hutchings', with a long horizontal stroke extending to the right.

NEIL HUTCHINGS  
Director of Power Systems and Energy Storage