

Frances Warburton
Partner, Energy Systems
Ofgem
9 Millbank
London
SW1P3GE
29 November 2016

Dear Ms Warburton,

Re: “Charging arrangements for embedded generation” dated 29 July 2016.

Background:

Tees Valley Combined Authority (TVCA) was created in April 2016 to drive economic growth and job creation in the area. It harnesses the economy-boosting powers of Tees Valley’s five local councils (Darlington, Hartlepool, Middlesbrough, Redcar and Cleveland and Stockton) and Tees Valley Local Enterprise Partnership to elevate partnership working between the public and private sectors to a new level in order to create an even more effective approach to building a stronger Tees Valley.

Tees Valley is home to a number of nationally important business sectors, including: process industries and advanced manufacturing, both of which are energy intensive. In addition, Tees Valley has existing strengths in electricity generation, which not only serves local demand but also the wider national market. The importance of electricity generation has been noted as a key priority within the refreshed Strategic Economic Plan, the Industrial Strategy for the Tees Valley (2016) and the following comments reflect the Plan.

Key Issues:

We note in paragraph 1 your concern that the current charging arrangements “are preventing a level playing field” between different types of **plant**. However, we believe that competition takes place between **companies** and that all companies are equally free to invest in Embedded Generation (EG) plants. To use a manufacturing example as an analogy, it would be unreasonable for companies which have invested in one form of infrastructure to deliver their products to customers to argue that they are at a disadvantage to their competitors who have identified a cheaper solution. Nor would it be reasonable for them to argue that if part of their infrastructure became stranded/obsolete that their competitors (particularly new entrants) should provide financial compensation. In our example, the stranded infrastructure represents the sunk NGC costs for capacity, which is arguably not used (and certainly not paid for) as a result of EG’s offset of demand below the grid supply point.

In seeking a solution we must start with the root cause of the problem. The existing TNUoS (more specifically the demand Triad) arrangement worked well for much of the last decade. Then a perturbation occurred as the number of renewables projects grew and they favoured distribution network operator (DNO) connections mainly because of their smaller plant capacities and the greater number of connection nodes available on the DNO systems. This initiated a process of reducing net demand from the transmission system which was further exacerbated by additional embedded generation which resulted in a vicious cycle of an increased Triad price (compounded by the €2.50 /MWh limit). **The current demand charging mechanism is becoming 'unstable'** (meaning a small random perturbation does not damp down, but instead grows further). It would be unreasonable for Ofgem to now remove Embedded Benefit from investors in existing EG plant who have made their investments in good faith in what is generally considered to be one of the world's most stable regulatory environments. However we also take the view that these same investors should not receive an excessive windfall arising from forecast growth of the demand residual component over the period until 20/21.

We therefore believe the demand residual component should be frozen at the current level until a thorough review of the transmission charging arrangement (in the form of a Significant Code Review) can occur. The current arrangements are too long standing, have significant investment based on them, and have strategic significance to regional economies such as the Tees Valley for such a quick fix approach to be adopted.

We also suggest that Ofgem should address the root cause of the problem, which is the skyward trajectory of the TNUoS demand charge. Addressing that issue would be a direct and first order improvement for customers.

We observe the timing of this, in the build up to the capacity market auction to be unsettling both to prospective and existing investors in our area alike. We therefore urge Ofgem to act swiftly to reassure them and establish some certainty in this matter.

Tees Valley Combined Authority.