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Open Letter: Charging arrangements for embedded generation

To whom it may concern,

Thank you for the opportunity to respond to this consultation. This response is on behalf of Statera Energy Limited.

We would first like to draw your attention to the significant investment that has been made by numerous developers at the distributed level. Investments like these are invaluable to UK plc at this time, and casting substantial doubt in this area is causing damage to investor confidence. We therefore urge Ofgem to: release a timely response to this open letter to stabilise the industry; and, not make any drastic changes without thorough, impartial evidence being presented.

We are concerned that decisions which impact embedded generation are being determined by CUSC signatories, most of whom would gain a commercial advantage should embedded generation be removed from the market. Further, any significant change to the embedded benefit regime would impair the future of the embedded generation industry, which when coupled with the concerns about the ever increasing cost of connecting to the DNO network (discussed below) would force generation to connect to the transmission network – a significant benefit to all TO parties involved in these discussions. We note from National Grid's most recent TNUoS 5 year forecast total transmission revenue is set to increase from £2.7b in 2016/17 to £3.79b in 2020/21 – over £1 billion of additional charges on the consumer, which would increase substantially to make up the energy shortage should embedded generation be forced out the market. These changes are a detriment to consumers: not only due to the resulting higher clearing prices in the capacity market, but as the minimal connection charges and disappearing use of system charges (TNUoS) both seen on the transmission network will encourage more generation at the fringes of the Transmission network – thus increasing the size of the network, and cost to the consumer, but also the Transmission revenues, and therefore National Grids/TO returns.

Regarding the workgroup discussions, we believe that both workgroup options being presented are drastic, substantial, and unjustified changes that would cause irreversible damage to existing and future Embedded Generators, Demand Side Response market participants and investors who have committed substantial investment in the Great Britain Electricity Market. That said, we acknowledge the substantial rise in the benefit is also unjustified (an unintended consequence of the €2.5/MWh European Regulation passing cost onto the Demand Residual and spiralling costs offshore) and requires addressing, however the entire/substantial removal of the embedded benefit is not justified. Considering the complexity of the various issues and the need for a thorough review it is not acceptable to rush a modification through in such short timescales in the lead up to capacity auctions.

As mentioned above, we would like to draw Ofgem's attention to the ever-increasing cost of being a distributed connected market participant, and encourage a full review of the comparative costs and benefits of being either Transmission connected or Distribution connected in the UK. Again, we would turn to recent National Grid evidence supporting the removal of the Small Generator Discount (see Embedded Benefit Open

Letter, April 2014) that showed the average 132kV transmission connectee paid £1.19/kW compared with an average of £15.03/kVA for a 132kV distribution connectee. Considering the substantial fall in transmission Generation Residual (i.e. the amount paid by transmission connected generation) since this 2014 National Grid assessment it is clear that Distributed Connected Generators were not only at a substantial disadvantage previously, but are in a much worse position today. According to page 14 of the consultation this continuous decrease in monies paid by Transmission Generators will result in the consumer *paying* transmission connectees £671.4m a year (Generation residual) by 2020/21, an amount which dwarfs that being paid via the embedded benefit. It appears clear that the current signals used to incentivise/dis-incentivise generators as to where they should connect/operate on the network are not functioning effectively - the existing signals are so heavily diluted they are not giving Transmission connected parties appropriate indication as to where they should locate projects. To improve this for distribution connected parties we support the increase and enhancement of the locational element of the embedded benefit (/demand signal). Furthermore Page 21 of the consultation discusses some of the access to market issues faced by distributed generation, further highlighting the un-level playing field. We urge Ofgem to review the market signals being given to market participants to ensure cost-reflectivity (particularly at a regional level), but in a way that considers the fundamental issues such as charging structures, which these modifications do not attempt to address.

There are clearly a number of regulatory issues which are linked via various methodologies, and to adjust just one factor without the others would be deliberately un-competitive and irresponsible in the run up to the Government capacity auctions. Particularly when there is already an un-level playing field between transmission and distribution, continuously reducing transmission charges, and CMP261 demonstrated Ofgem's willingness to provide regulatory certainty/security to current and future transmission connectees in this area. We therefore urge Ofgem to undergo a fuller, holistic review that aims to level the playing field and give the appropriate signals to generators as to where they should connect to the network. Clearly exporting GSPs is an area which requires immediate attention. It is not clear to us why an embedded site at an exporting GSP receives an embedded benefit – obviously this depends on the definition of an exporting GSP, but a site which exports more than is needed locally at peak cannot justify their need for an embedded benefit. Further, we believe Ofgem should review the way in which Demand zones are used to calculate the netting of demand (e.g. the whole of Scotland is split into 2 demand zones – does this make sense to allow a generator in the very north of Scotland net off with Demand near the central belt?)

We do not believe the changes raised by these modifications would benefit the consumer, as discussed in paragraph 3.8.8 of the consultation. The removal of embedded benefits would reduce competition and increase capacity market clearing prices and wholesale peaking prices. They may also result in material investment being required in the transmission networks. None of these market wide impacts are considered in the modification consultation.

There are also some wider points Ofgem must consider:

- Parties with multiple year agreements from 2014/15 t-4 auctions risk losing their embedded benefits if P265 is approved, so the economic response must be to find a way to terminate their agreements (leaving the market short in 2018/19/20);
- Going into T-4 2016 all embedded generators will now have to assume that the embedded benefits are worth less than expected by investors, who acted in good faith, which undermines their future plans and therefore may reduce competition in the auction;
- While signals can advantage embedded or transmission connected plant, both are having significant problems getting connection capacity and this problem sits with Ofgem; and

In order to dis-connect the calculation of the embedded benefit from being increased by European regulation (that is increasing the Demand residual) we support the WACM put forward by Green Frog et al. as it seems fair until a wider review is conducted, whilst also giving certainty for upcoming auctions. We note that National Grid's April 2014 Embedded Benefit review did not support any changes to the Demand Residual, and therefore believe the Green Frog modification could be better justified by using the Demand Residual at the time of this National Grid review (£35/kW, in April 2014) in addition to the locational tariff.



Please do not hesitate to contact myself should you have any questions,

Yours faithfully,

Tom Vernon
Director,
Statera Energy Limited