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Date: 24 January 2019

Small generator discount - Decision to modify Standard Licence Condition C13 (Adjustment to use of system charges (small generators)) of the electricity transmission licence

We have decided to extend the discount for small generators in Scotland as set out in Standard Licence Condition C13 (Adjustment to use of system charges (small generators)) (SLC C13) of the electricity transmission licence (the Licence) from 31 March 2019 to 31 March 2021. It also applies to offshore generators which are under 100 MW and are 132 kV transmission connected. This letter describes the reasons for our decision. This further extension should not be taken as providing any assurance as to the continuation of the discount beyond 31 March 2021 if no decision on enduring charging arrangements for embedded generation is made before the new expiry date.

We are publishing the formal Modification to the transmission licence and non-confidential responses to our consultation on our website alongside this letter.

Background

The discount referred to as the small generator discount was introduced¹ by the UK Government at the time of BETTA² in 2005. The aim of the discount was to create a level playing field between under 100 MW 132 kV *transmission* connected generators in Scotland, and those that are *distribution* connected at 132 kV in England and Wales. It also applies to offshore generators which are under 100 MW and are 132 kV transmission connected. Generators connected at 132 kV to the distribution system in England and Wales and with a capacity of below 100 MW are called smaller embedded generators and do not pay generation transmission charges. Until April 2018 smaller embedded generators were treated as negative demand³ for the purposes of transmission charging and typically received a benefit from suppliers for reducing their demand transmission charges. Since April 2018, this has been replaced by the Embedded Export Tariff (EET), described below. Small generators connected to the 132 kV network in Scotland do not receive the EET, and pay generator transmission charges.

¹ https://www.ofgem.gov.uk/sites/default/files/docs/2004/05/6951_9604.pdf

² The British Electricity Trading and Transmission Arrangements (BETTA), joined the wholesale market in England & Wales to that in Scotland.

³ The volume of embedded generation is taken off the total demand volume to create a net demand for the purposes of transmission charging

The level of the small generator discount was determined by Ofgem in 2005 and is 25% of the sum of the generation and demand residual⁴ Transmission Network Use of System (TNUoS) tariffs in a given charging year. This is recovered from demand consumers across GB.

The discount was time limited and was originally set to expire on 31 March 2008 to allow time to develop enduring charging arrangements for embedded generators. The expiry date has been extended four times to date due to different interacting projects. The current expiry date set out in paragraph 5 of SLC C13 is 31 March 2019.

The implementation of our decision on Connection and Use of System modification proposals (CMP) 264/265 in April 2018⁵ has changed the treatment of embedded generators in TNUoS charging. Embedded generators (including those connected at 132 kV in England and Wales) are no longer treated as negative demand but receive the Embedded Export Tariff (EET), which is a payment based on the locational element of demand tariffs, a credit for avoided infrastructure reinforcements at the Grid Supply Point (GSP), and a declining proportion of the residual charge. The EET is floored at zero so that it can never be a cost to generators. Whilst the benefit to embedded generators has reduced, there remain differences to the treatment of 100 MW 132 kV transmission connected generators in Scotland. The reforms to the TNUoS demand residual are being phased in over the period 2018/19 to 2020/21.

The Targeted Charging Review⁶ (TCR) was launched in August 2017 to address concerns that the current framework for residual charging may result in inefficient use of the networks, and to keep other embedded benefits under review. We published our TCR minded to decision and Impact Assessment for consultation on 28 November 2018. We are consulting on enduring changes to the arrangements for the charging of the residual element of network charges, including the option of recovering residual charges from final demand only and the removal of some of the remaining other non-locational embedded benefits.

Our proposal

On 28 November 2018, we proposed to modify SLC C13 by amending the expiry date of this condition from 31 March 2019 to 31 March 2021.⁷ Appended to that letter was a formal Notice under section 11A of the Electricity Act 1989 setting out our proposed modification of the Licence.

Responses to our statutory consultation

We received 17 responses to our statutory consultation of which 15 were supportive of our proposal to extend the current expiry date of 31 March 2019 to 31 March 2021. Of the two responses not expressing support, one was opposed to the extension of the small generator discount at all, and proposed that the discount should be calculated on a different basis if it were to be extended. The other respondent would not be opposed to the extension only if the small Generator Discount was calculated on a different basis, related to the EET.

Those who supported our proposal said that the different treatment between sub 100 MW generators connected at 132 kV in Scotland, and those in England & Wales continued to lead to a distortion which the small generator discount addresses in part. Others said that it is appropriate to maintain the current approach to the discount until related charging reform work is completed.

⁴ The residual is the element of the TNUoS charges that is collected from all users on a socialised basis and does not vary by location. It is determined to recover the correct amount of total revenue and to ensure the correct split of recovery between generators and suppliers.

⁵ <https://www.ofgem.gov.uk/publications-and-updates/embedded-benefits-impact-assessment-and-decision-industry-proposals-cmp264-and-cmp265-change-electricity-transmission-charging-arrangements-embedded-generators>

⁶ https://www.ofgem.gov.uk/system/files/docs/2017/08/tcr_scr_launch_letter.pdf

⁷ <https://www.ofgem.gov.uk/ofgem-publications/143676>

The respondent who opposed the extension expressed a view that the small generator discount no longer fulfilled its original purpose. The respondent said that the concept of the small generator discount introduces undue discrimination between similar parties connected to different parts of the transmission network and that this is reason in itself for not continuing it. We consider that other distortions remain between the treatment of smaller and larger generators and have proposed reforms to the relating to non-locational Embedded Benefits through the TCR. We believe it is proportionate to continue to the small generator discount in its current form whilst these reforms are considered and enacted. The same respondent said that the original conditions set by Ofgem and Government for the removal of the small generator discount have been met following the implementation of CMP264/5 and therefore the discount should already have been removed with effect from April 2018. We do not agree that the transmission demand residual embedded benefit has been resolved as of April 2018 since the phasing of the residual charge will occur over three years.

The two respondents who suggested a different calculation methodology said that the phased Transmission Demand Residual (used in the calculation of the Embedded Export Tariff as introduced by CMP 264/5) should be used in the calculation of the Small Generator Discount, instead of the Transmission Demand Residual. The proposed logic is that the Embedded Benefit is now related to the phased residual rather than the Transmission Demand Residual.

This approach would reduce the value of the small generator discount in the 2019/20 charging year, and would potentially lead to a negative value in the 2020/21 charging year. We think that this would not constitute an “extension” of the small generator discount and would not align with our intent to maintain the current arrangements ahead of implementation of the Targeted Charging Review.

Future of the small generator discount

Of those who supported the extension, many of those said that we should not rule out further extension of the small generator discount.

Some said that the small generator discount should be continued until Ofgem’s Electricity Access Reform project is concluded. On future expectations, a number of respondents consider that this and previous decisions to extend the discount create a legitimate expectation that if changes to charging arrangements for Embedded Generation are not developed by 31 March 2021, then the discount will be extended again. Four respondents said that any restriction to the small generator discount without a fair system in place will have a negative effect on the viability of renewable energy sources and, therefore, UK’s climate change targets.

We wish to make it clear that there should be no legitimate expectation of the discount continuing beyond the current extension and that any future decision on extending the discount will be made based on the evidence available to us at that time.

We do not agree that the small generator discount should continue until the Electricity Access Reform project is concluded, since the small generator discount is based on residual charges, not the forward looking charges which are the subject of the Access project. Even if the implementation of the reform of non-locational embedded benefits were to be delayed beyond 1 April 2021, we do not currently see a case for further extension of the small generator discount.

Our decision

We continue to believe that it is appropriate to maintain the status quo arrangements whilst we progress with our proposed TCR reforms.

We have decided to modify SLC C13 by amending the expiry date of this condition from 31 March 2019 to 31 March 2021. Appended to this letter is a formal Notice under section 11A of the Electricity Act 1989 setting out our decision notice to modify SLC C13.

The discount was introduced to provide a level playing field for small 132 kV connected generators in Scotland while industry developed enduring arrangements for transmission charging for embedded generators. These arrangements continue to be developed via the TCR. In our view, it is appropriate that the discount remains in place while this work continues.

For the avoidance of doubt, when the new TCR arrangements are developed, we would envisage using our power under paragraph 4 of SLC C13 to direct the designated sum under the small generator discount be made zero, if appropriate.

Yours faithfully,

Andrew Burgess
Deputy Director, Energy Systems Transition