



## Targeted Charging Review: a consultation

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Judith Ross  
Ofgem  
9 Millbank,  
Westminster,  
London,  
SW1P 3GE

5<sup>th</sup> May 2017

Dear Judith,

### **Background**

InterGen welcomes the opportunity to respond to this important consultation. We are a truly independent generator active in the UK market with a track record of developing, constructing and operating large scale thermal power generation projects. We have been active in the market since the 1990s and therefore bring a unique perspective to this consultation. InterGen is owned by two major international investor classes which the Government is seeking to attract to invest in UK infrastructure namely: pension funds (Ontario Teachers' Pension Plan); and strategic investors from the People's Republic of China (China Huaneng/Yudean).

InterGen is one of the UK's largest independent generators, operating a portfolio of three flexible gas-fired power stations totalling 2.5GW; an investment of some £2.1bn. These stations are located at Rocksavage (Cheshire), Spalding (Lincolnshire) and Coryton (Essex).

In December 2016, at the T-4 auction, InterGen won a fifteen-year capacity market agreement to construct a 300MW OCGT at our existing Spalding site. InterGen is also positioned, subject to Capacity Market award, to build new CCGT projects at sites at Spalding (Spalding Energy Expansion) and Essex (Gateway Energy). The new CCGT stations, which are "shovel-ready", will together cost around £800million to construct and create around 3,000 jobs over their three year build programmes.

The consultation is particularly important as our Capacity Market pricing and ability to attract investment in our 300MW OCGT at Spalding are premised on the existing electricity charging arrangements pertinent to transmission connected projects. Any material impact on the OCGT raises fundamental questions about the long term viability of that project and also the UK's attractiveness to attract investment, with fundamental policy "flip flopping" having a material adverse impact both at project and national level.

## **Response to Consultation Questions**

*Question 1: Do you agree that the potential for residual charges to fall increasingly on groups of consumers who are less able to take action than others who are connected to the system, is something we should address?*

Yes, this is an appropriate consideration of any potential SCR. Much discussion, particularly at the regulator's workshop held in April, has focussed on the elasticity of customers and their ability to 'up sticks and move'. Elasticity is a principles based consideration and the protection of, in particular, vulnerable residential customers is important.

*Question 2: If so, why do you think, or do not think, action is needed?*

InterGen supports Ofgem's review of the level of demand residual payments currently afforded to embedded generation – this is a clear market distortion and is contrary to a truly fair and competitive market taking place.

As per the principles outlined to be adopted in this process, this is not 'fair' and is not a level playing field. Market distortions should be addressed in the fullest way and in a timely fashion.

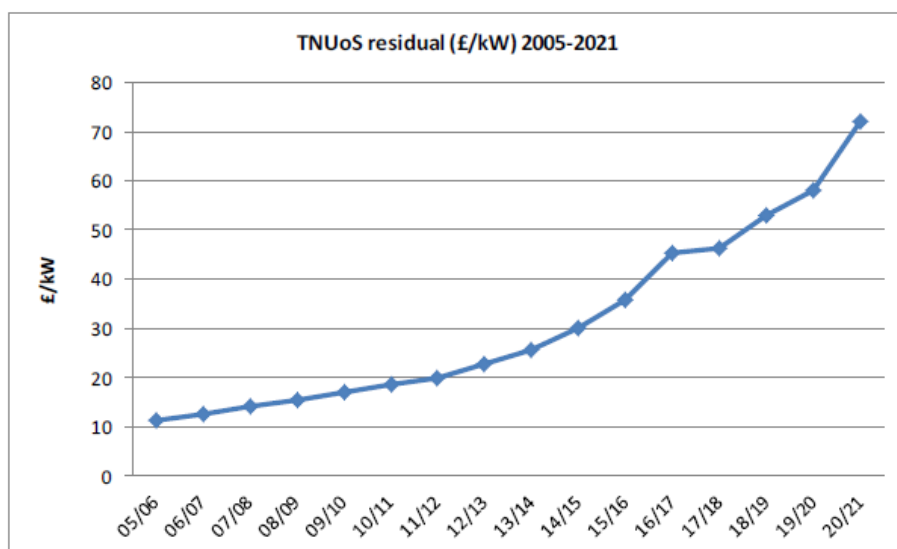
InterGen would stress caution in making significant changes to the methodology driving generation residual tariffs. InterGen can pay testament to the importance of current TNUoS methodology and forecasts the strong degree of investor certainty it provides for the development of new transmission connected infrastructure. In particular, the consultation is particularly important as our Capacity Market pricing and ability to attract investment in our 300MW OCGT at Spalding are premised on the existing electricity charging arrangements pertinent to transmission connected projects. Any material impact on the OCGT raises fundamental questions about the long term viability of that project and also the UK's attractiveness to attract investment, with fundamental policy "flip flopping" having a material adverse impact both at project and national level. InterGen has already spent considerable sums on the OCGT project (+£10 million) and a material adverse change to transmission charging puts into question the viability of the project and our further new planned investment in the UK.

Further changes to the transmission charging regime following the sweeping changes of Project Transmit (P213) will further dent investor confidence in investing in large scale transmission connected assets over concerns that the charging regime is under perpetual review. We also note that the Project Transmit changes were relatively recent, which gave industry the confidence to make Capacity Market pricing decisions with very low risk of material changes being made in the short to medium term.

Likewise for existing thermal assets connected to the transmission system. Forecasted TNUoS charges provided by National Grid as recently as February 2017 for the next five years are question marked and to be replaced with something that could be significantly different with material economic consequences for the ongoing economic viability of this type of asset.

*Question 3: We are proposing to look at residual charges in a Significant Code Review. Are there any elements of residual charges that you think should be addressed more urgently? Please say why.*

As highlighted above, the residual charging arrangements for embedded generation which is addressed in CMP 264/265 is a significant market distortion that should be addressed more urgently than any wider SCR. As per Ofgem's minded to decision letter on this modification, the process of EG netting off supplier's demand level, and sharing in the value of this TNUoS demand residual (TDR) cost avoidance, has a current average value of £45/kW which is expected to rise to £72/kW by 2021.<sup>1</sup>



*Figure 1- TDR payments available to smaller EG*

The size and increase in TDR payments has already and continues to cause a number of distortions:

- **Dispatch** – Smaller EG generate out of merit to ensure they hit the triad periods;
- **Wholesale price** – By running out of merit, the wholesale market price is distorted and artificially damped at peak times;
- **The Capacity Market** – Smaller EG have a competitive advantage when bidding into the CM, reducing their possible bid prices;
- **Inefficient investment in generation capacity** – A large financial incentive to locate on the distribution system despite it possibly not being the most efficient place to locate;

*Question 4: Are there elements of the approaches in other countries that you think could be appropriate for GB residual charges?*

N/A

<sup>1</sup>

[https://www.ofgem.gov.uk/system/files/docs/2017/03/minded\\_to\\_decision\\_and\\_draft\\_impact\\_assessment\\_of\\_industrys\\_proposals.pdf](https://www.ofgem.gov.uk/system/files/docs/2017/03/minded_to_decision_and_draft_impact_assessment_of_industrys_proposals.pdf)

*Question 5: Are there other approaches that you know about from other jurisdictions, that you think offer relevant lessons for GB?*

N/A

*Question 6: Do you agree that our proposed principles for assessing options for residual charges are the right ones? Please suggest any specific changes, or new principles that you think should apply.*

The proposed principles for assessing options for *demand* residual charging seem fair and appropriate.

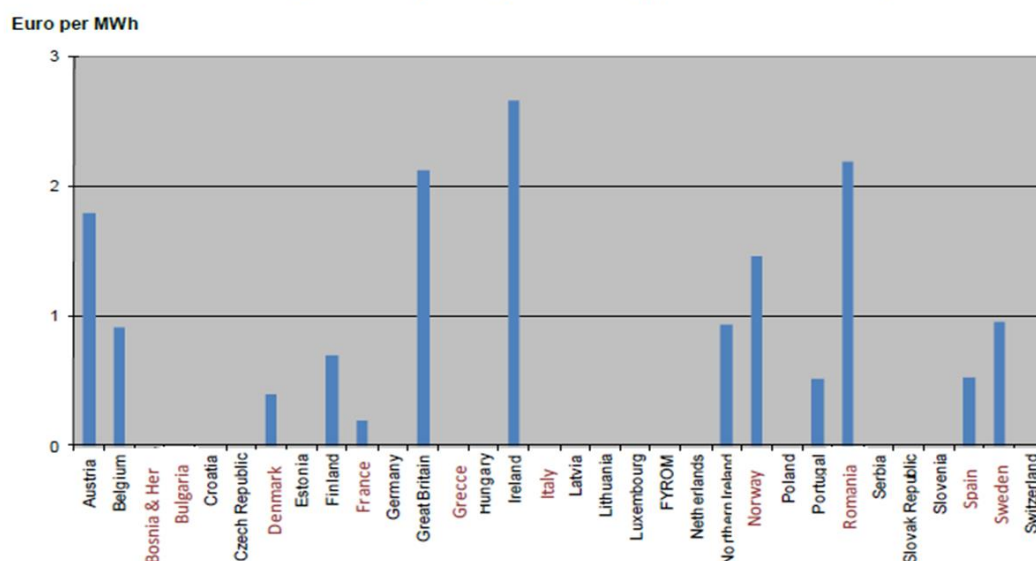
*Question 7: In future, which of these parties should pay the transmission residual charges: generators (transmission- or distribution-connected), storage (transmission- or distribution-connected), and demand, and why? What proportion of these charges should be recovered from each type of user?*

The current proportional split, with regards to transmission residual charges, seems fair. InterGen believes the issue is not with the generation residual charge but the wider TNUoS tariff more broadly. Increasing amounts being recovered through residual charges is an indication that the other aspects of the tariff are not cost reflective and providing adequate and robust locational signals – they are dwarfed by the scale of the residual charges.

InterGen raised a CUSC modification proposal in 2014 (CMP 227) which sought to address the split of these charges and we proposed 15:85 Generation: Demand split. The current split of 27:73 we believe has a distorting impact on competition and is a clear outlier when compared to other European transmission systems (shown in Chart 4 below):

- No change means GB generators face higher costs than European competitors.
- Generators are increasingly at a competitive disadvantage as the EU internal market develops with electricity interconnection (installed interconnector capacity forecasted at 14GW by 2023)

**Chart 4. Range of G components paid in 2013 by producers across Europe.**



We would be supportive of a review of this split.<sup>2</sup>

*Question 8: In future, which of these parties should pay the distribution residual charges: generators (transmission- or distribution-connected.), storage (transmission- or distribution-connected), and demand, and why? What proportion of these charges should be recovered from each type of user?*

We do not believe that transmission connected generation should be exposed to the distribution residual.

*Question 9: Do you support any of the five options we have set out for residual charges below, and why?*

InterGen would support option D – *gross kWh consumption*. This charging methodology would address the distortion that has arisen with embedded generation receiving disproportionate revenues from cost saving through lowering suppliers' net demand. It also promotes innovative behaviour – demand users are incentivised to lower their energy usage through means likely to include; energy efficiency, demand side response, smart meters, consumer behaviour etc.

*Question 10: Are there other options for residual charges that you think we should consider, and why?*

N/A

*Question 11: Are there any options that you think we should rule out now? Please say why.*

N/A

*Question 12: Do you think we should do further work to analyse the potential effects of the charging arrangements for smaller EG (called 'embedded benefits')?*

InterGen believes that satisfactory work has been carried out on the issues surrounding charging arrangements for sub 100MW EG. 25 different proposals were presented to Ofgem as part of the CUSC modification process each outlining different issues and concern and possible remedies. The CUSC modification process has already been running for a year and a swift conclusion is required to this recognised market distortion.

*Question 13: Do you think changes are needed to the current charging arrangements for smaller EG, and when should any such changes be implemented?*

Please see our response to question 3, InterGen believes that the TNUoS demand residual payment for embedded generators is a substantial market distortion requiring immediate attention.

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<sup>2</sup> [https://www.ofgem.gov.uk/sites/default/files/docs/2015/09/cmp227\\_d\\_0.pdf](https://www.ofgem.gov.uk/sites/default/files/docs/2015/09/cmp227_d_0.pdf)

*Question 14: Of the embedded benefits listed in our table, do you think that any should be a higher or lower priority?*

Demand Residual payment, currently valued at £45/kW and rising, is the largest recognised distortion and should be treated as a priority. Furthermore this current distortion is negatively impacting other policy areas namely the capacity market.

*Question 15: Do you think there are other aspects of transmission or distribution network charging which put smaller EG, or any other forms of generation or demand, at a material disadvantage?*

N/A

*Question 16: Do you agree with our view that storage should not pay the current demand residual charge, at either transmission or distribution level?*

N/A

*Question 17: Do you agree with our view that storage should not pay BSUoS on both demand and generation?*

N/A

*Question 18: Which of the BSUoS approaches describe is more likely to achieve a level playing field for storage?*

N/A

*Question 19: Do you think the changes in this chapter should be made ahead of any wider changes to residual charging that may happen in future? Do you agree with our view that these changes should be implemented by industry through the standard code change process?*

InterGen would suggest that with clear issues of market distortion, such as Ofgem's minded to position for CMP 264/265 and the lowering of TDR payments to EG, there should be immediate corrective action taken. The proposed changes to storage should be considered carefully and thoroughly as part of the wider planned SCR.

*Question 20: We would welcome your thoughts on the potential make-up of a CCG. Please refer to the potential role, structure, prioritisation criteria and assessment criteria.*

InterGen agrees with the proposed role, structure and criteria. It is important that the CCG reflects a holistic view of the industry and there is proportional representation from all aspects of the market. In addition, in the interests of accountability and transparency, it is important that communication is frequent and meaningful with the wider industry as to how the work of the group is progress – it should not be a closed door process.

*Question 21: Do you agree with our proposed delivery model, including its scope?*

The proposed delivery model seems appropriate and allows flexibility for issues that need urgent attention, or can be addressed promptly, to occur outside of the SCR timescales.

*Question 22: Do you agree that our proposed SCR process is most appropriate for taking forward the residual charging and other arrangements for smaller EG discussed in this document?*

InterGen believes the treatment of charging arrangements for smaller EG should progress earlier than the broader SCR. Over 25 different proposals were offered to the regulator as part of CMP 264/265 and the modification process has already been underway a year. The distortion needs a settled and prompt solution applied to it.

We highlight that we are making investment decisions based on the existing TNUoS regime that impact transmission connected assets and that any material adverse impact on these investments could bring into question project viability and raise questions over the attractiveness of UK plc as a place to invest.

I would welcome the opportunity to discuss the above with you given its importance.

Yours sincerely

A handwritten signature in black ink, appearing to read 'L Mackay', with a stylized flourish at the end.

Lisa Mackay  
Trading and Commercial Director  
InterGen UK