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Energy Systems Integration
Office of Gas and Electricity Markets
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London
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27 November 2017

Dear Andrew,

RE: UK Power Reserve response to Enabling the competitive deployment of storage in a flexible energy system: changes to the electricity distribution licence

Submitted via email

Please find here UK Power Reserve's response to Ofgem's consultation on the proposed changes to the electricity distribution licence.

Context of response

UK Power Reserve is the leading provider of secure, flexible, low carbon electricity and services to the UK power market. With an 823MW portfolio of decentralised thermal power generation and battery storage assets, we help keep the country's electricity system balanced and resilient. Our fast-ramping, low-cost assets are located across England and Wales, improving competition, contributing to security of supply, and delivering better value to consumers.

Summary

- As well as not being able to operate storage, DNOs (including IDNOs) should not be automatically enabled or allowed to own storage other than in exceptional circumstances. Such circumstances would include the provision of uninterruptible power supplies at substations and time-limited purposes of emergency restoration and maintenance.
- UKPR stresses that the EU Third Energy Package requirements for the unbundling of transmission networks is an appropriate model to apply as a minimum standard for DNO separation from storage ownership and operation.
- UKPR stress that the prohibition on owning and operating storage should apply to all assets currently owned and/or operated by DNOs. The proposed exclusion from the prohibition for already existing DNO-owned and operated islanded system generation and storage is not justifiable and could set a dangerous precedent.
- We do not support the *ad hoc* approach that Ofgem envisage using for existing DNO-owned storage assets, and do not think that a case-by-case treatment is a suitable solution. To ensure that ownership

and commercial operations are kept separate, as well as achieve the lowest cost to consumers, these assets should be sold.

- A transparent application process for the right to an exemption should be used. This should be based on the key criteria defined by Ofgem in the licence to ensure that consistency is maintained.

Should you have any questions, please do not hesitate to contact Alessandra De Zottis at alessandra.dezottis@ukpowerreserve.com.

Kind regards,

Alessandra De Zottis
Regulatory Affairs Manager
UK Power Reserve

Proposed new condition in the electricity distribution licence

Question 1: Do you agree that the proposed new condition will ensure legal unbundling of DNOs from the operation of storage that benefits from an exemption to hold a generation licence?

UKPR welcomes Ofgem's efforts to tackle the concerns in relation to the significant negative effects on competitive markets of network operators owning and operating storage.

We share Ofgem's concerns, that if monopoly network companies participate in competitive markets they would be abusing their position, and potentially distort competition and deter new market entrants. In addition, participation of natural monopolies in competitive markets would not represent an advantage to consumers, as lower costs are only guaranteed in an open, competitive market.

As such, UKPR fully supports Ofgem's conclusion in the Smart Systems and Flexibility Plan that network operators should not own or operate storage. UKPR stresses that the EU Third Energy Package requirements for the unbundling of transmission networks is an appropriate model to apply as a minimum standard for DNO separation from storage ownership and operation.

However, UKPR feels that the proposed new condition does not fully ensure legal unbundling of DNOs from the operation of storage below 100MW. More stringent conditions should be clearly included in the proposed modification of Section 11 of the electricity distribution code. If Ofgem is to effectively facilitate the creation of a fully functional market for storage, it would be a retrograde step to allow networks to participate.

Ofgem's aim is to address an already grey area, whereby generation below 100MW does not require a generation licence and DNOs can own small scale storage. To truly prevent DNOs or their subsidiaries from distorting flexibility markets, rules must be set out in the distribution code. Exemptions should be clearly defined and limited to uninterruptible power supplies at substations and to time-limited emergency restoration and maintenance purposes, provided that such tools and devices do not export electricity to the network.

Furthermore, UKPR calls for a comprehensive rule, setting both operational and ownership separation between the DNO activities and all-scale storage assets. Network companies control and maintain the infrastructure where flexibility services are traded. As Ofgem have rightly pointed out, network operators can restrict the activities of market participants by hampering their network access. Should they be allowed to own storage assets, as is currently the case for some LCNF-funded pilot projects, they can also guarantee preferential treatment and access to the assets they own, gaining an unfair advantage.

Question 2: Do you agree that the same principles of unbundling should apply to IDNOs? Do you have any views on the application of the specific new condition proposed here applying to IDNOs?

Yes, UKPR agrees that IDNOs should be subject to the same principles of unbundling; as their role is to develop, operate and maintain local electricity distribution networks and are connected (directly or indirectly) to DNOs.

IDNOs are regulated like DNOs, and are mainly extensions to the DNO networks, serving new housing and commercial developments. Should they be exempt from the unbundling rule, this would represent a severe fault

in the system: they could take up an aggregation role for the areas they serve and could be used by DNOs to gain an unfair advantage over market players participating in an open, competitive market.

Question 3: Do you agree that DNOs should be able to directly own and operate small-scale storage for the purposes of providing uninterruptible power supplies (UPS) at substations? Do you agree that DNOs should be able to directly own and operate small-scale storage for the time-limited purposes of emergency restoration and maintenance? Do you think DNOs should be able to directly own and operate storage for any other specific applications?

UKPR agrees in principle with DNOs owning and operating small scale storage exclusively for the purposes of providing uninterruptible power supplies at substations and time-limited purposes of emergency restoration and maintenance. We appreciate that DNOs play a key role in maintaining safe, efficient and reliable networks and we welcome tools that would facilitate this purpose, provided that such tools and devices do not export electricity to the network.

However, contrary to Ofgem's proposal, such specific exceptions should be included in the new licence condition, instead of being defined within an accompanying guidance document. Although the guidance document is legally binding, we would want to avoid a plethora of changes to the guidance document that would be subject only to stakeholders' consultations.

UKPR calls for clarity and transparency of the allowed exceptions to the prohibition for DNOs to operate storage. Any change in such exceptions should therefore be limited and should follow a systematic process.

DNOs should not be able to directly own and operate storage for any other specific applications. UKPR recommends limiting the number of exception to a strict minimum: all other circumstances whereby DNOs claim to be allowed to own and operate storage should undergo a thorough application and approval process, with notification and consultation provided to all interested stakeholders.

Question 4: Do you have any views on the treatment of existing islanded system generation currently owned by DNOs? Do you have any views on the treatment of future use of DNO owned and operated generation of storage in similar island situations?

UKPR stresses the need for the new prohibition proposed by Ofgem to apply to all assets currently owned and/or operated by DNOs.

UKPR feels the proposed exclusion from the prohibition for already existing DNO-owned and operated islanded system generation and storage is not justifiable and could set a dangerous precedent. Considering the risks already identified and recognised by Ofgem, UKPR would appreciate a stricter approach to truly tackle the issues and risks of DNOs owning and operating storage.

The proposed requirement only for new sites and replacements of assets at the existing sites to apply to Ofgem for permission to operate is not realistically sufficient to tackle and solve the issue. We also do not support a system that would allow already existing DNO-owned and operated islanded system generation and storage to apply for permission to operate because they do not meet the unbundling requirement.

UKPR believes that the only suitable approach is for DNOs to be required to sell their existing generating and storage assets to open market participants.

Also in the context of islanded networks, DNOs should not be allowed to continue operations and should go to the market tendering the sale of their assets, and subsequently procure the flexibility services they need. An open and competitive procurement system is sufficient to provide the amount and type of capacity required in the area. Market participants like UKPR can provide the required flexibility services at the lowest cost to consumers.

On a related note, we are surprised to see that Ofgem have not addressed any questions regarding the existing treatment of existing DNO-owned and operated storage. This is a crucial controversial element that stakeholders should be consulted on, and UKPR has a clear vision on the most appropriate treatment of such assets. We do not support the *ad hoc* approach that Ofgem is envisaging and we do not think that a case-by-case treatment of existing DNO-owned storage assets is a suitable solution to implement the new prohibition.

As Ofgem have rightly pointed out, consumers' money has already been spent on these projects and UKPR urges the regulator to act to avoid further costs: consumers paid for trial projects aimed at understanding how storage could provide thermal, voltage, and reactive power to support the distribution networks. Now that most of these projects have ended – allowing DNOs to gather the knowledge of their networks' needs – they should sell their assets for full ownership and commercial operativity separation.

The best value for money for consumers is provided not by monopolies but by the open market, where services are procured competitively. UKPR, as the leading provider of reliable, flexible and low carbon power services to the UK electricity market has been able to grow its portfolio of small-scale, local thermal power generation and battery storage assets at the lowest cost to consumers.

Ofgem should therefore provide the adequate binding rules for all DNO-owned and/operated storage assets to allow the full application of the prohibition principle.

Guidance document

Question 1: What are your views on the three high-level criteria proposed as the basis for assessing applications for consent? Do think there are other criteria which should also be included?

UKPR in principle agree with the three high level criteria that the DNO must demonstrate have been met before the regulator would provide consent for them to operate a storage facility directly.

With regards to the first condition whereby DNOs must demonstrate that the market is not able to provide an efficient solution, UKPR would like to stress the need for Ofgem to request that the DNO had run open and competitive tenders to the market. Simply signalling its needs ahead of time would not be sufficiently transparent to allow distributed energy resource providers to respond and offer their services.

The other criterion that requires clearer and more prescriptive value is the expectation on DNOs to put in place arrangements, other than legal unbundling, that would ensure the risks of discrimination or distortion to the market are effectively managed.

Question 2: Do you have any other views on the scope or content of the proposed guidance document?

UKPR does not support Ofgem's approach that sets out a range of circumstances where DNOs are not required to submit any applications for specific consent. We understand that, as DNOs would not be required to apply, the exception (i.e. the possibility to operate generation or storage assets) would be granted automatically. This does not reflect the rationale of the prohibition, as DNOs would have rather accessible routes to avoid the need to ask for permission to Ofgem.

DNOs ownership and operation of generating and storage assets should be allowed only in catastrophic market failure circumstances. As such, the proposed circumstances whereby DNOs are only required to be satisfied they comply with the unbundling principle, or whereby they put in place appropriate commercial arrangements with third parties, are not remotely sufficient to guarantee an effective prohibition.

Question 3: Do you have any views on the process that should apply to the assessment of applications?

UKPR expects the application process to be as standardised as possible to guarantee a fair and transparent assessment of the requests. Should DNOs be allowed to submit a discretionary set of information, it would be extremely challenging to evaluate their applications.

We would expect Ofgem to provide at least a formal template for applications and a set of documentation proving some statements (e.g. around unbundling). UKPR would like to stress the risk of incurring in a range of situations that would require verification but that could be easily dismissed by DNOs with the "commercially sensitive information" card.

As a further necessary requirement, all relevant stakeholders should be given the opportunity to engage via formal consultation.

Reporting and monitoring

Question 1: Do you have any views on reporting requirements for DNOs that own/operate storage assets?

UKPR in principle agrees with Ofgem that there isn't any specific need to have oversight of arrangements between DNOs and an independently owned and operated storage provider. However, Ofgem should require well-defined and comprehensive proof from the DNOs of the arrangements put in place for open and transparent procurement processes.

We urge Ofgem not to underestimate the level of risk of market distortion when not appropriately monitoring DNOs and their involvement with ownership of storage assets and other flexibility services. There are instances whereby DNOs have contracted commercially for flexibility services from an independently owned and operated storage provider, only after the storage asset the DNO developed and owned has been previously sold to that given provider. This can also include an agreement of guaranteed capacity at certain times and period of the year from such independent storage provider.

Furthermore, UKPR stresses the need for Ofgem to review the business separation rules already set out in the DNO licence to fully reflect the new set of rules and obligations set out in the proposed new Condition 43B. This

is particularly necessary as the regulator itself recognises that the unbundling regime for DNOs requires them to be legally separate from the operation of generation – but does not require separate ownership.

In this context, UKPR would also like to stress the need to extend the requirement to hold a generation licence to generators with a capacity of less than 100MW. Avoiding another exemption would help the Regulator properly tackle situations that could easily lead to market distortions.

Question 2: Are there any particular types of data that, if published, could facilitate entry of competitive parties? Is there any other information or data that you think DNOs hold about the deployment of storage on their networks that they could usefully make public?

UKPR, as a competitive provider of the flexibility services required by DNOs, has been dealing with challenging situations relating to the visibility of the needs of the DNOs: there are many “public tenders” where certain DNOs have not published the amount of capacity required in a given area. At times, signals from the demand side of the market could be difficult to assess due to a lack of publicly available information.

Ofgem should therefore establish a clear reporting and monitoring mechanism to make sure DNOs effectively signal areas of potential need as well as test the market with transparent, open and competitive tenders, accessible to all competitive markets.