



**Consumer
Focus**
Campaigning for a fair deal

Consumer Focus response to DECC's consultation: Improving Grid Access

November 2009

About Consumer Focus

Consumer Focus is the independent champion for consumers across England, Wales, Scotland, and (for postal consumers), in Northern Ireland. We operate across the whole of the economy, persuading businesses and public services to put consumers at the heart of what they do.

Consumer Focus was formed on 1 October 2008 through the merger of three organisations – energywatch, Postwatch and the National Consumer Council (including the Scottish and Welsh Consumer Councils). We are a statutory organisation that works in a devolved setting, with work priorities varying across different parts of the country, by all working to common strategic goals.

Through campaigning, advocacy and research, we champion consumers' interests in private and public sectors by working to secure fairer markets, greater value for money, and improved customer service. We have a particular focus on the interests of consumers in markets that are 'designated' by Government as requiring additional consumer advocacy. Currently these include energy and postal service consumers.

Consumer Focus also has a commitment to work on behalf of vulnerable and disadvantaged consumers, and a duty to work on issues of sustainable development.

Overview

- It is evident that whatever model is chosen to improve grid access, constraint costs will increase and that consumers face increased prices
- We believe that the impact on current and future consumers must be kept at the heart of the decision about new transmission access arrangements
- We have kept our comments at a high policy level and for the reasons outlined below do not support any particular model at this time
- Consumer Focus has identified five key principles to guide the Government's decision and to ensure that consumer's needs are considered paramount

Consumer Focus response to key issues

We welcome this opportunity to respond to the Department of Environment and Climate Change (DECC) consultation on Improving Grid Access. The technical and complex nature of the proposed new arrangements is highlighted within both the DECC consultation documents and the report by Frontier Economics called '*An assessment of the potential impact on consumers of connect and manage access proposals*' which was recently released by Ofgem.

Given the technical nature of the documents it is difficult to assess the exact impact for consumers. We note that the Ofgem document was released on 6 November with little time to properly assess the report prior to the closing date of this consultation. Indeed Ofgem's report has attracted some criticism by industry experts¹ who state that some of the assumptions in the report are questionable and open to challenge.

Therefore, given that Consumer Focus does not have the technical expertise to comment on the complex detail of the proposed arrangements we will keep our comments at a broad policy level.

We understand that at present there is a 'queue' of approximately 60GW of new electricity generation capacity (including renewable generation) seeking connection to the grid, with connection dates as late as 2023. Consumer Focus agrees that this is a problem if GB is to meet its climate change targets for 2020 and beyond.

We know this consultation has come about because industry and the regulator Ofgem could not agree on a successful outcome to address transmission access. As such Government decided to intervene using powers under the *Energy Act 2008*. The DECC consultation documents state that Government intends to intervene to deliver improved arrangements for access to the electricity system for new generation investments.

In addition under the Act the Secretary of State must ensure that any grid access framework must be structured in the manner best calculated to protect the interest of existing and future electricity consumers. The overall costs, and indeed overall impact on consumers, of any new arrangements we hope will therefore be an important consideration in the Government's final decision.

We also note that under EU law transmission and distribution charges should not discriminate against renewable energy sources and also under the Electricity Directive for the EU Third Package member states must protect vulnerable consumers (by March 2011). These are two important factors for the Government to keep at the forefront of its mind while making decisions about the new transmission access arrangements.

DECC is consulting on proposals that would introduce a new transmission access regime in GB. Three models are under consideration, all variants of the 'connect and manage' approach and they are:

- The 'socialised' model costs would be shared between all users of the network and ultimately borne by consumers

¹ Cornwall Energy *Energy Spectrum* Issue 209. Page 12.

- The 'hybrid' model which would target some but not all additional constraint costs on new generators
- The 'shared cost and commitment' model that offers choice to new and existing generators to commit to the network in return for greater certainty over charges, or to opt out and be exposed to additional constraint costs

What is evident is that consumers will ultimately bear the costs of the new arrangements. Some industry experts have spoken anecdotally that the measures are expected to put £1 per year on the average household bill by 2020.

This cost seems fairly minimal, however, Consumer Focus is increasingly concerned that this is just one of a number of elements that the energy consumer, especially the domestic consumer, is expected to bear. It seems that consumers must bear the full brunt of the cost of the Government's environmental policies, with seemingly little regard for a shared burden across taxpayers and shareholders as well.

Given our remit to help protect disadvantaged and vulnerable consumers we have focused on the issue of price increases. Energy bills will be rising in the medium term (and will continue to do so in the long term) as a result of, for example, renewable obligations, smart metering, the Carbon Emissions Reduction Target (CERT), Feed-in Tariffs (FiT) and network costs more generally. In addition Government has recently announced a three per cent clean coal levy on consumer bills. It is vital that consumers do not become overly burdened or the de facto solution to all financial deficits. A plethora of energy price increases have serious implications for all consumers but more specifically for those more vulnerable energy consumers.

Figures released by DECC in October 2009 predict that the number of fuel poor households in England could rise to 4.6 million this year. Assuming fuel poverty in Scotland, Wales and Northern Ireland rose at the same rate as England, this translates to 6.6 million fuel poor households in the UK. We are therefore already facing a fuel poverty crisis. Ofgem's recent Project Discovery scenarios and DECC's Low Carbon Transition Plan proposals considered alongside the new arrangements to deal with transmission access problems, will undoubtedly make the crisis even worse unless there is a substantial change in policy to address the issue.

The Government cannot consider the decision about transmission access and impact on consumers in isolation. There needs to be acknowledgement and consideration of combined cost increases.

We agree that it is crucial that Great Britain has adequate future generation capacity and that there is sufficient capacity to access the grid. We know there have been dramatic increases in the actual and forecasted cost of constraint management and all the indications are that a 'connect and manage' approach favored by Government will exacerbate increasing prices further.

In terms of general price increases, by funding the transition to a secure low carbon energy economy through energy bills rather than general taxation, people on low incomes or in hard-to-heat homes are paying disproportionately for a strategy that has broad societal and environmental benefits.

Consumer Focus thinks that Government should recognise that significant public expenditure is required, rather than expect consumers to foot the entire bill of transition. Benefits and burdens must be proportionately borne between all parties – business, tax payers and consumers. We often hear the argument that it does not matter whether consumers or taxpayers pay the bill – the bill still has to be paid. However, general taxation represents a more progressive method of raising finance than levies on bills, particularly given that energy costs represent a significant proportion of low income household's expenditure.

Key principles to guide decision

Given that consumers will pay for the connection of new generation to the grid, whatever the model chosen by Government, we find it difficult to support any of the proposed models. A full impact assessment as to what this will mean for consumers is required.

We outline below five key principles which should be taken into account by Government when making its decision about which model to progress:

1. That increased constraint costs and the impact on consumers' bills are not considered in isolation, rather considered alongside all other increases and levies being implemented to fund the Government's environmental objectives
2. That the impact of increasing energy bills on the vulnerable and fuel poor are kept at the heart of any decision made by Government
3. The Government should recognise that significant public expenditure is required, rather than expect consumers to foot the entire bill of transition to a low carbon economy. Benefits and burdens must be proportionately borne between all parties - shareholders, tax payers and consumers
4. If some increased constraints costs are to be passed onto consumers, this should be done in a fair, affordable, clear and transparent way and a full impact assessment should be undertaken before a final decision is made
5. Accepting the above four principles, Consumer Focus would support a model that facilitates efficient use of the transmission system – regardless of generation mix, **without** discrimination to renewable generators

Refer to annex one for our answers to DECC's more specific questions and further information.

Annex one: Response to specific questions

Scope of intervention:

- 1. Taking into account the need for a timely solution to access delays for new generation projects, and the costs associated with taking action, do you agree with the targeted intervention planned by Government?**

Yes. The issues of mounting constraint costs and increasing pressure to ensure that we have an infrastructure that is capable of meeting the UK's climate change targets mean that a timely solution is critical. However, we would caveat that with an appreciation of frustration expressed by the industry (particularly those involved in the Connection Use of System Code change processes) that considerable resource was invested in a process that very nearly led to a workable solution. It would be a shame if, as a result of Government intervention, the efforts of the industry and the analysis completed went to waste, or if industry participants were dissuaded from becoming involved in industry change processes.

However, as mentioned in the body of our response a detailed and full impact assessment of the impact on consumers should be undertaken prior to a final decision being made.

- 2. Do you have any evidence to indicate that other issues should be considered as part of these access reforms, rather than, for example, through the normal governance procedures?**

It is appropriate that other issues aren't included within the scope of the Government's intervention (especially given the tight timescales in place for identifying and implementing a solution). However, steps should be taken to ensure that the solution dovetails efficiently with other things going on (other TAR principles, smart grids etc). Also, further consideration should be given to address the issue of new plant joining the queue on a speculative basis? (see paragraphs 5 and 7 page 18 of the DECC document).

- 3. From what date do you consider the enduring arrangements should apply?**

Consumer Focus does not have a specific view on this, although clearly there is benefit in implementing a solution that delivers certainty for investment decisions sooner rather than later.

Industry grid access proposals:

- 4. Do you agree with our initial assessment of the impacts of the industry grid access proposals (including on the Fourth Model, which was not formally considered by the industry process)?**

Yes, although it would be helpful to see a more detailed and specific breakdown of the anticipated financial and any other impacts of each of the models on consumers. It would also be useful to see some more detailed analysis of the anticipated impact on competition of each of the models (given that increased competition is cited as one of the benefits to offset the increased costs). It would also be helpful to include more discussion on the split of costs between future and current consumers, ie who faces the cost burden and when?

There is no mention of the potential threat of legal action in response to any of the options if they are viewed by market participants as discriminatory. Could this have a big impact on implementation timescales?

5. Do you agree with our initial view that we should focus on models based on a Connect & Manage approach?

This is difficult to fully support without a more detailed analysis of costs and benefits, although on the surface the cited benefits of this model do seem reasonable. However, we have concerns about each model eg increased constraint costs that the Connect & Manage approach is likely to cause and lack of incentive on existing generators to modify their operations to reduce constraint costs (particularly under the hybrid model).

Analysis of models for consultation:

6. Do you agree with our initial assessment of the impacts of the different Connect & Manage models?

See response to question 4. More specific information on the anticipated costs and benefits of each model would be useful. For example the impact assessment quotes costs of £633 million for each model, so it is difficult to differentiate on the basis of costs to consumers.

We look forward to more detailed analysis of potential deferred recovery mechanisms to enable some discussion on the spread/impact of costs between current and future consumers.

7. Are there any further impacts of these models you consider ought to be borne in mind?

As stated above, more detailed analysis and specific information on the costs and benefits of each model would be useful.

8. What generation mix do you consider these various models would be likely to lead to by 2020?

No view, given we are not technical experts in this area.

9. In your view, what impact on overall generation and transmission costs would the various models be likely to lead to and by when?

No view, given we are not technical experts in this area.

10. Do you have any evidence of any risks or unintended consequences as a result of any elements of these models?

No, given we are not technical experts in this area.

11. Do you agree with the Government's initial view that a model along the lines of Connect & Manage (Hybrid) is likely to best meet our objectives?

No. It is difficult for Consumer Focus to commit without further analysis of costs v benefits (as detailed above). We recommend that the key principles mentioned in the body of our response are used to guide the decision of Government.

Detailed questions on the models for consultation:

12. In relation to the Connect and Manage (Hybrid) model, what balance do you consider to be appropriate between socialisation and targeting of additional constraint costs? How should these costs be recovered? Would a form of locational BSUoS be an appropriate mechanism for targeting a proportion of the additional constraint costs? Should this apply to everyone behind an identified constraint or be targeted solely at new generation opting for a Connect & Manage connection? Are there other means for targeting constraint costs (apart from locational BSUoS) which the Government ought to consider?

It is Consumer Focus's view that any model implemented should include provisions to ensure that costs in their entirety are not automatically passed on to consumers. Any costs that are passed on should be proportionate, fair and transparent.

There might be some potential benefits of locational BSUoS. It might help to resolve some of the market power issues previously seen above the Cheviot boundary and also send signals to encourage existing generators to modify their operations to reduce constraint costs (ie a polluter pays type incentive). More assessment is needed before any decision is made on locational BSUoS.

13. If targeted solely at new generation – would this pass the discrimination test? Also, is there a danger that this could disincentivise new investment and lead to security of supply/renewable target issues?

Refer to answer to question 5.

14. Do you consider that any element of user commitment beyond existing requirements is necessary as part of the solution? If so, what form should this take? Should this be for a fixed period (eg five years as envisaged in the Shared Cost & Commitment model) or for a flexible period?

Consumer Focus believes that an optimal solution should include an element of user commitment. This will provide the flexibility for guaranteed access at a cost, good use of market forces, plus will also create the stability required to encourage investment.

15. Do you consider that some kind of deferred recovery of some element of constraint costs should form part of the solution? If so, what form could this take? What proportion of costs should have deferred recovery and over what length of time?

In principle yes. Deferred recovery would provide a useful mechanism for ensuring that a proportion of the costs of investment are incurred by consumers. Depending on the period of deferment this could include future consumers. It is difficult to be specific on proportions and timescales – a cost benefit analysis of a range of combinations would be useful.

16. Do you have views on whether a deferred recovery mechanism would be allowable under International Accounting Standards and if so how this might work?

No view, given we are not experts in this area.

17. Are there any other features of the models described which you consider could be amended or improved?

See responses above. Additional detail on costs (specifically those likely to be incurred by consumers), benefits, anticipated impacts on competition and potential deferred recovery mechanisms would be useful.

Other issues:

18. Do you agree with our initial view that the enduring access regime should apply equally to distributed generation in categories (a) and (b)? What would be the benefits and impact, in terms of facilitating access to or efficient use of the transmission system, of applying the new regime to this distributed generation? What interactions do you see between the models set out in this consultation and distributed generation? Do you agree that any further amendments to the treatment of distributed generation should be progressed through the industry-Ofgem governance process?

Consumer Focus supports any solution that, at a proportionate cost to consumers, facilitates efficient use of the transmission system – regardless of generation mix. However, there are obvious benefits to any characteristics of the model which better facilitate access for distributed renewable generation. Given the strict timescales that DECC are working to, it seems prudent to allow further amendments to the treatment of distributed generation to be progressed through the industry-Ofgem governance process. This would allow thorough analysis of potential solutions. However, Consumer Focus would seek reassurance that this issue would be picked up by the industry and worked through to a conclusion within reasonable timescales.

Summary questions:

19. Are there any other issues that Government should bear in mind to ensure the sustainable and effective implementation of changes to support the efficient access to and use of the transmission system?

It would be useful to better understand DECC's thoughts on how National Grid could be encouraged and given incentives to ensure that the transmission system is used in the most efficient way possible and also that constraint costs are kept to a minimum. It is encouraging to see recent reductions in constraint costs against National Grid's original projections. Are there any more initiatives that National Grid could make use of to sustain the trend?

20. Do you have any specific comments on licence and code amendments required to implement these models?

No not at this time.

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Improving Grid Access

Contact: Abigail Hall, Senior Policy Advocate

Tel: 020 7799 7934

Email: Abigail.hall@consumerfocus.org.uk

www.consumerfocus.org.uk

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Edited by Alistair Moses, Consumer Focus

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can contact Consumer Focus via Text Relay:

From a textphone, call 18001 020 7799 7900

From a telephone, call 18002 020 7799 7900

Consumer Focus

4th Floor

Artillery House

Artillery Row

London SW1P 1RT

Tel: 020 7799 7900

Fax: 020 7799 7901

Media Team: 020 7799 8005 / 8006