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Ørsted response to regulatory treatment of CLASS as a balancing service in RIIO-ED2 network price control

20 March 2020

Our ref. CLASS/Ofgem

Dear Edwin,

The Ørsted vision is a world that runs entirely on green energy. Ørsted develops, constructs and operates offshore and onshore wind farms, solar farms, energy storage facilities, and bioenergy plants, and provides energy products to its customers. Globally, Ørsted is the market leader in offshore wind and it is constructing the world's biggest offshore wind farms off the East Coast of the UK. Its UK offshore wind farms generate enough clean electricity for over three million UK homes. Headquartered in Denmark, Ørsted employs 6,500 people, including over 1,000 in the UK.

We welcome the opportunity to respond to your consultation on the regulatory treatment of CLASS. Ørsted believes that the provision of balancing services is a key enabler for a decarbonised energy system and as such, we support a fair market place where all participants can compete on an equal footing. We are concerned that your minded-to position would allow Distribution Network Operators (DNO) to potentially significantly distort the market and deter future commercial interest and innovation from new entrants and existing providers alike. Although we recognise that there may be short-term benefits to today's consumers as DNOs may currently have a means to provide these services to the Electricity System Operator (ESO), it will harm the long-term interests of tomorrow's consumers if competition is absent. We recommend Ofgem to adopt a more holistic approach to create an open market that is attractive to new entrants and promote competition within a level playing field, and we set these views out in more detail below.

A level playing field for all ancillary service providers

There will be a conflict of interest that may be difficult to mitigate, especially in a future where DNOs potentially transition to become a Distribution System Operator (DSO) and come into direct competition with other network users. Further, as DNO revenue is regulated for operating its network assets, it is difficult to justify why DNOs should receive additional revenue from the same assets.

Additionally, setting this precedent today would allow the future DSO to contract with itself for provision of system services. We understand this has been part of the rationale for the ESO and Transmission System Owner (TSO) split, and the same concern still holds for DNOs.

In the future world where energy production is expected to become more decentralised, we are concerned that your minded-to decision to allow DNOs to participate in commercial services would be harmful to competition. This is because we do not think network operators should compete with network users who are their customers.

In addition, we think DNOs' financial structure gives them an unfair advantage when competing with other businesses, e.g. Firm Frequency Response (FFR) and Fast Reserve (FR) providers. Having regulated revenue streams from monopoly infrastructures means that DNOs can enjoy a cheaper source of finance, which becomes distortive against other service providers who are exposed to market rates.

Coordinated procurement of ancillary services from both transmission and distribution networks will improve efficiency

We support the creation of a centralised flexibility market which facilitates the efficient procurement of ancillary services from all possible sources and operated by the ESO. We are concerned that liquidity may become limited if these services are separately procured by individual DNOs and subsequently sold to the ESO. This may result in distortive local prices and increase costs for consumers in a local pricing zone with less liquidity and less competition.

The ESO already procures a range of ancillary services for the operation of transmission network, we think that the possibility of extending the procurement to the distribution network should not be ruled out.

Long term consumer benefits and impacts need to be fully understood

With their regulated revenues, having DNOs also participating in commercial activities could be damaging to competition and risks the interests of tomorrow's consumers, especially without thorough analysis and scoping of unintended consequences.

We are not entirely convinced that the CLASS study has sufficiently assessed the full-service impact on consumers. When voltage control actions are taken, consumers will experience a lower rate of power flow. There will be an impact on consumers, e.g. negative impact on productivity for industrial users. When energy users' consumption is altered in the manner that CLASS operates, there will be consequential impacts on the suppliers' imbalance position. A standard industry practice is that suppliers will pass any additional charges back to their customers. This can be commercially challenging when multiple customers and suppliers are involved, and that the complexity could deter suppliers from contracting with these customers.

It is also worth considering the impact of the network security (e.g. voltage head/foot room) when active voltage control actions are regularly carried out by DNOs, and whether such activities would undermine other more critical DNO services to prevent blackout.

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Overall, Ørsted is concerned that long term consumer interests will be compromised if DNOs are permitted to compete in a commercial market by taking advantage of its natural monopoly position. We disagree that DNOs should be allowed to offer CLASS services to the ESO. However, we welcome industry effort to continue to explore options for a more open and transparency ancillary service market for network users, across both transmission and distribution levels.

If you have any questions or would like to discuss our response, please contact me directly on 078 7969 7812 or olixi@orsted.co.uk.

Yours sincerely

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