

dti

*REGULATION OF OFFSHORE
ELECTRICITY DISTRIBUTION*

Government Response to
the Consultation Paper on a
Draft Class Exemption Order
for Offshore Distribution
Systems

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GOVERNMENT RESPONSE TO THE CONSULTATION PAPER ON A DRAFT CLASS EXEMPTION ORDER FOR OFFSHORE DISTRIBUTION SYSTEMS

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CHAPTER 1 : INTRODUCTION & DECISION

Summary

- 1.1 On 22 November 2006, the DTI published a consultation document on the regulation of offshore distribution networks¹, which invited views on a proposal for the exemption by class of offshore distribution networks and set out a deadline for responses.
- 1.2 Interested parties likely to be affected by the Order were invited to comment on the proposal over a period of 28 days. These included holders of licences for electricity generation offshore, licence-exempt offshore electricity generators, holders of distribution and transmission licences in GB, the GB System Operator (GBSO), as well as other interested parties. We also gave statutory notice to Energywatch and the Gas and Electricity Markets Authority.
- 1.3 The consultation closed on 20 December 2006. This document sets out the Government's conclusions from this consultation and a timetable for next steps.
- 1.4 Copies of the consultation paper, RIA and individual responses are available on the DTI website: www.dti.gov.uk. Please contact Katherine Watson on 020 7215 2891 or via email at katherine.watson@dti.gsi.gov.uk for further information.

Why DTI conducted the Consultation

- 1.5 The Government decided in March 2006 that the appropriate model for the regulation of offshore transmission systems is by a price control approach, similar to onshore. This decision means that post commencement of sections 89 to 92 and 180 of the *Energy Act 2004* ('the 2004 Act') there will be a regulatory framework for offshore transmission (high voltage lines), including offshore licences.
- 1.6 In order to provide a clear, consistent and enduring offshore grid regime for all connections, DTI has considered the regulatory position of low voltage offshore connections (distribution systems). DTI published an Open Letter to industry on 20 November 2006 clarifying the position of high and low voltage offshore connections².
- 1.7 Because of the relatively small scale and currently limited number of low voltage connections offshore, the DTI considered it appropriate and proportionate for persons distributing electricity only from offshore generating stations to benefit from a class exemption from the requirement to hold a distribution licence. In doing so, the DTI aims to minimise the regulatory burden on a small number of companies, whilst avoiding any potential risk to the safe and secure operation of the GB electricity system.
- 1.8 The Consultation therefore sought representations on the DTI's proposal to add, by Order, a new class 'D' for offshore distribution to the existing distribution class exemptions in Schedule 3 to the *Electricity (Class Exemptions from the Requirement for a Licence) Order 2001* ('the 2001 Order'). All operators of distribution connections that only convey electricity from offshore generating stations would qualify for this exemption. It is subject to conditions in the Order.
- 1.9 The proposal affects the operators of low voltage connections offshore, including the six operating generating stations offshore (Blyth, EMEC, Scroby Sands, Kentish Flats, North Hoyle and Barrow) and all planned low voltage systems connecting offshore generating stations to the GB grid.

¹ The Consultation paper is available at: <http://www.dti.gov.uk/files/file35593.pdf>

² The Open Letter is available on the DTI website at: <http://www.dti.gov.uk/files/file35598.pdf>

- 1.10 The consultation anticipated that the proposed class exemption would apply to operators of low voltage connections from future offshore generating stations, subject to the Government keeping under review the case for exempting operators of low voltage connections offshore in light of how the network develops, for example, if the class exemption regime could no longer secure the integrity of the onshore electricity network.

Summary of responses to the Consultation

- 1.11 In total, 16 written responses were received. All respondents agreed their responses could be made public. These responses were supplemented by discussions with individual parties. The DTI would like to thank all those who contributed their views. All responses received, views expressed and questions raised during this period were carefully analysed and considered against the aims of this policy.
- 1.12 Responses were received from Generators, Transmission Owners, the GBSO, Distribution Network Operators (DNOs), a trade association, consultant, Regional Development Agency, and Energywatch. A full list of these stakeholders is provided in Annex A and their replies can be viewed on the DTI web site.
- 1.13 A large majority of responses supported the proposal, with just one response preferring an alternative option of granting individual exemptions. In particular, respondents supporting the proposal believed that:
- i. This approach is the simplest, most timely, most cost effective and proportionate response in current circumstances.
 - ii. The exemption would minimise the regulatory burden, administration and cost associated with connections to shore for offshore generators operating in a limited capacity.
 - iii. The difference between onshore and offshore distribution networks (no demand connected and point-to-point connections) justified a 'lighter' regulatory regime.
 - iv. The existing distribution class exemptions set a pragmatic approach to follow.
 - v. A class exemption would provide existing and new projects with immediate regulatory certainty, reducing risk for developers.
 - vi. A licensing regime would require substantial and time-consuming work, which would not be appropriate or proportionate, so long as it is only a small number of low-output generators that are connected to the licence-exempt systems and there is little impact on demand customers and the integrity of the system onshore.
- 1.14 There were no strong arguments against the establishment of the class exemption. However, it was noted by respondents that certain issues meant that the exemption should be kept under review post-implementation:
- i. Changes to the number and level of output of generators connected to offshore distribution systems, particularly any change in impact on demand customers and the integrity of the system onshore.
 - ii. Emerging needs of future technologies, such as wave and tidal generation, for a more co-ordinated approach to offshore distribution network development.
 - iii. Continued enforcement of contractual arrangements on design standards and information provision by licensed distributors.
 - iv. The possibility of incorporating the offshore distribution regime into the offshore transmission regime once established.
- 1.15 Some respondents addressed all or most questions in the consultation; others focused only on those questions concerning matters of particular interest to them. Respondents also raised a range of specific issues, each of which is discussed in turn in Chapter 3. The RIA has been updated in light of responses and can be viewed on the DTI website.

Decision and Next Steps

- 1.16 The Government has decided that the proposal to establish a class exemption for offshore distribution is the correct approach, given the limited number of offshore distribution systems and the low volume of electricity conveyed through them. This approach should minimise the regulatory burden on these companies whilst ensuring the safety and quality of supply to consumers.
- 1.17 The Government will therefore proceed with implementing the exemption through an amending Statutory Instrument, having taken on board comments received. The Order will come into force on 6 April 2007.

CHAPTER 2 : RESPONSES

- 2.1 This section summarises the comments made by respondents to each of the 3 questions raised in the consultation paper and provides a Government response. Each question is taken in turn below.

Question 1

Should the application of Schedule 3 to the Electricity (Class Exemptions from the Requirement for a Licence) Order 2001 (“the 2001 Order”), which provides that certain classes of distributor are exempt from the requirement to hold a distribution licence, subject to certain conditions, be amended to include a new class D for all offshore distributors? Please set out the reasoning behind your response.

- 2.2 A clear majority of respondents agreed with the proposal to introduce the class exemption for offshore distributors, although a number of comments and questions were raised. Responses to each point are set out below.

Response	Number of Responses
Yes	10
Yes, subject to comments made	4
No	1
No comment	1
Total	16

Geographic scope of the proposed class exemption

- 2.3 One respondent, Scottish and Southern Energy, noted that they agreed with the proposal in principle, but only in respect of connections from generating stations located in the territorial sea and Renewable Energy Zone (REZ). The respondent suggested that an exemption was only needed offshore because of the absence of a licensed DNO to offer a point of connection adjacent to the generating station. They argued that therefore the class exemption should not apply to connections from generating stations located in internal waters as, in their view, these connections were already within the scope of onshore distribution licences.

Government response

- 2.4 The Government notes in response that we are not proposing to introduce a class exemption specifically for offshore distribution because of a lack of distribution licensees, but because we believe a class exemption is the appropriate regulatory approach for offshore distribution at present. Furthermore, the distribution licensing regime is not exclusive. For example, onshore distribution licensees presently co-exist both with other distribution licensees, where Independent DNOs compete with DNOs within their licensed areas, and with the existing distribution class exemption regime (classes A, B and C). As a result, we do not consider that internal waters should be excluded from the scope of the proposed class exemption for offshore distribution, regardless of whether or not an existing distribution license covers internal waters.

Definition and interpretation of ‘distribution’

- 2.5 Two respondents, United Utilities and Tony Cotton, agreed with the proposal in principle, but questioned the Government’s approach as, in their view, the planned low-voltage connections for generating stations should be considered part of the generating station, rather than separate distribution systems. As such, they did not believe a class exemption would be required at present. However, they agreed that if the connections were to be regulated as distribution, a class exemption would be appropriate.

- 2.6 A further respondent, AMEC, put forward the same argument that these connections were part of the generating stations and concluded that as a result the class exemption was inappropriate. They commented that if all offshore generating stations are metered at their onshore connection point, then in their view any 11kV or 33kV infrastructure would be part of the generating station, and that licensing requirements for distribution would not apply. They proposed instead that where connections were distribution systems, the Government should consider granting individual exemptions rather than a class exemption. They considered that a class exemption might still be appropriate, depending on the number of generating stations involved in the future.

Government response

- 2.7 We have noted the responses on the definition of distribution, but as the DTI's open letter to industry on the regulatory position of offshore connections (published on 20 November 2006) made clear, the Government considers that low voltage offshore connections are distribution systems, as defined in the Electricity Act 1989 ('the 1989 Act') (as amended by the Utilities Act 2000).

- 2.8 "Distribute" is defined in section 4(4) of the 1989 Act (as amended by the Utilities Act 2000):

"distribute", in relation to electricity, means distribute by means of a distribution system, that is to say, a system which consists (wholly or mainly) of low voltage lines and electrical plant and is used for conveying electricity to any premises or to any other distribution system;"

- 2.9 "High voltage line" and "low voltage line" are defined in s.64(1) of the 1989 Act (before amendment by s.180 of the 2004 Act)³:

"high voltage line" means—

- (a) in relation to England and Wales, an electric line of a nominal voltage exceeding 132 kilovolts;*
- (b) in relation to Scotland, an electric line of a nominal voltage not less than 132 kilovolts,*

and "low voltage line" shall be construed accordingly.

- 2.10 Section 64 of the 1989 Act (as amended by the Utilities Act 2000) further defines "electrical plant" and "electric line" as:

"electric line" means any line which is used for carrying electricity for any purpose and includes, unless the context otherwise requires—

(a) any support for any such line, that is to say, any structure, pole or other thing in, on, by or from which any such line is or may be supported, carried or suspended;

(b) any apparatus connected to any such line for the purpose of carrying electricity; and

(c) any wire, cable, tube, pipe or other similar thing (including its casing or coating) which surrounds or supports, or is surrounded or supported by, or is installed in close proximity to, or is supported, carried or suspended in association with, any such line;"

"electrical plant" means any plant, equipment, apparatus or appliance used for, or for purposes connected with, the generation, transmission, distribution or supply of electricity, other than—

(a) an electric line;

³ S180 EA 2004 amends the definition of high voltage line in s64(1)(a) so that a relevant offshore line (as defined in s64 subsection (1A)) of a nominal voltage of 132 kilovolts or more is high voltage.

(b) a meter used for ascertaining the quantity of electricity supplied to any premises; or

(c) an electrical appliance under the control of a consumer;”

Question 2

Will the proposed conditions (provision of information to Ofgem and no distribution directly to domestic consumers) be sufficient to provide for the safe operation of the distribution networks? If not, what alternative or additional provisions might be put in place to achieve this aim?

Response	Number of Responses
Yes	10
Yes, subject to industry code modifications	1
No view	5
Total	16

- 2.11 The majority of respondents, including those who considered that these connections should not be regulated as distribution systems, believed the two conditions proposed would be sufficient to ensure the safe operation of the offshore distribution networks. A number of further comments were made, which are responded to below.

Contractual Arrangements

- 2.12 Three respondents, United Utilities, EON, and Centrica, commented that it would however be essential to maintain existing contractual arrangements between onshore licensed DNOs and the offshore generators.
- 2.13 Another respondent, the GBSO, considered that it would be necessary to safeguard current arrangements whereby the onshore licensed DNO ensures that certain technical requirements are complied with prior to the energisation of an embedded generator, regardless of whether they are connected directly or, as in this case, via a licence-exempt offshore distribution system. The GBSO suggested that minor modifications to the Grid Code and Connection and Use of System Code (CUSC) to achieve this outcome could be made through the normal industry code modification procedures, by exercise of the Secretary of State’s powers under the 2004 Act for modification of a code maintained in accordance with the conditions of a distribution or transmission licence, or by conditions attached to the class exemption order.

Government response

- 2.14 At present, a licensed offshore generator would be required to comply with the CUSC and Grid Code in order to ensure that the GBSO can carry out its licence duties in respect of the operation of the GB transmission system. Where the generator is both licence exempt and is embedded within a distribution system, the licensed DNO to which they connect is obliged under the Grid Code to ensure that the generator complies with certain Grid Code obligations⁴ through contractual arrangements with the generator.
- 2.15 CUSC 6.5.1 and Grid Code PC.3.3, CC3.4 and CC3.5 place an obligation on licensed distributors to identify before the energisation of an embedded generator’s connection to their system whether their connection would have a significant effect on the GB Transmission System, either in isolation or as part of the cumulative impact of a number of embedded generators connecting in a locality. If it is concluded that the embedded generator would trigger transmission reinforcement works, then National Grid and the host DNO would enter into an agreement for the relevant works. The DNO would also undertake not to energise the embedded generator’s connection until such transmission

⁴ These obligations are listed in the Grid Code in PC 3.3 and CC 3.4. CC 3.3 is also relevant.

works were completed. National Grid's response stated that as unlicensed offshore distributors would not be obliged to sign up to the CUSC, the risk of impact on the transmission system created by generators embedded in licence exempt distribution systems would not be adequately managed by the CUSC arrangements. These sections of the Grid Code also place obligations on licensed distributors relating to the provision of information and data to the GBSO relating to the connection and the generating station, as well as its compliance with design standards.

- 2.16 The Government agrees that it is appropriate for generators embedded in distribution systems to be treated consistently irrespective of whether they are connected to a licensed or exempt distribution system. We consider that the arrangements should facilitate compliance with relevant CUSC and Grid Code provisions by the licensed DNO in respect of generators connected to that distribution system via an exempt distribution system.
- 2.17 Three classes of distributor are currently exempted from the requirement for a licence under the 2001 Order. It is our understanding that these systems and generators embedded within them do not currently create a concern regarding compliance with the requirements set out above.
- 2.18 It is for market participants to consider if the class D exemption will have consequential impacts on the current Grid Code and CUSC drafting, which puts the responsibility for ensuring compliance with the requirements set out above on the onshore licensed DNO to which these systems ultimately connect, and how they should be amended to reflect the new regulatory framework offshore. In particular, whether to explicitly oblige the onshore DNO licensee to ensure this compliance of embedded generators who connect to their system via a licence-exempt distribution system prior to energising the connection between the licence-exempt and licensed systems. However, we agree with the GBSO that if non-compliance is a concern offshore, then it would be best addressed through modifications to the relevant codes using the normal procedures rather than through the class exemption. As a result, we have not made any amendments to the draft SI responding to this concern.
- 2.19 Any party (including a licence exempt distributor) who connects to the transmission system is required to have a contractual agreement with the GBSO. This contractual agreement would require compliance with the CUSC and Grid Code.

Provision of information to Ofgem

- 2.20 One respondent, EMEC, raised concerns regarding the potential under this condition for Ofgem to release into the public domain data which has been provided to EMEC as commercial in confidence.

Government response

- 2.21 It is important to note in response that Ofgem is constrained by section 105 of the Utilities Act 2000 "general restrictions on disclosure of information". Furthermore, we consider that this condition, which is included in other gas and electricity licence exemptions, assists the Authority in carrying out its functions, e.g. for ensuring non-discrimination, effective competition and the efficient functioning of the market, in particular the level of transparency and competition. We therefore do not consider that amendments should be made to the drafting of this condition.

Question 3

Do respondents agree with the costs and benefits outlined in the Regulatory Impact Assessment in Annex C? Are there any additional costs and benefits associated with the three options that have not been identified?

Response	Number of Responses
Yes	8
Yes, subject to corrections	1
No	2
No view	4
Total	16

- 2.22 A clear majority of respondents agreed with the costs and benefits cited in the RIA or had no view on this question. A number of comments were made, which have been reflected in the updated Final RIA.
- 2.23 One respondent, EDF Energy, suggested there was an inaccuracy in the calculated cost of carbon. The text explaining these calculations has been amended to explain better the methods used.
- 2.24 Another respondent, Centrica, observed that all GB electricity consumers, for whom security of supply is increasingly important, would be significantly disadvantaged if a long and costly process deterred potential developers of offshore distribution from coming forward.
- 2.25 The three respondents who considered these connections should not be regulated as distribution systems noted that as a result they disagreed with the benefits of introducing a class exemption. As one foresaw a much-reduced number of potential offshore distributors, they believed the costs of the individual exemptions route might be lower than a class exemption. Another noted that there might now be concern that certain onshore generation connections may require licences or exemptions, and that this concern may in itself create costs that might not otherwise have arisen.
- 2.26 Whilst one respondent, Centrica, noted that a class exemption would provide existing and new projects with immediate regulatory certainty, reducing risk for developers, another respondent, EON, noted that future marine demonstration projects could benefit from their distribution assets being held within an onshore licensee's asset base (and price control). The two wave and tidal testing centres (EMEC and SWRDA's WaveHub) however believed that the class exemption would be beneficial to wave and tidal developers.

CHAPTER 3: OTHER ISSUES

- 3.1 In addition to comments directly responding to the three questions posed in the consultation paper, respondents raised a number of specific issues of concern. Responses to each issue are set out individually below.

Interaction with individual Generation licence exemptions

- 3.2 One respondent, Tony Cotton, noted that the existing individual generation licence exemptions for offshore generators require the station to be connected to the 'total system'. He argued that as the exemption does not require that the stations be connected to a private distribution system, which in turn is connected to the total system, this made it clear that the offshore systems were part of the generating station.
- 3.3 Another respondent, Centrica, asked the DTI to clarify whether the same entity could have a generation licence exemption and a distribution licence exemption. They asked for confirmation that this would not invalidate the generator's licence exempt status or conflict with generation licence conditions.

Government response

- 3.4 The Government does not see a conflict between the existing generation exemptions and Class D. They relate to separate activities (generation and distribution) and therefore separate licensing requirements. We therefore do not see any reason why a company should not be able to benefit from a generation licence exemption and a distribution licence exemption at the same time, subject to their meeting the conditions contained in the exemptions, for example, not having directly connected domestic consumers.

Boundary between onshore and offshore systems

- 3.5 A respondent asked the DTI to clarify the boundary between the offshore and the onshore distribution network in the Exemption Order, as they believe this would increase transparency in the application of the Order.

Government response

- 3.6 The exemption applies to persons (other than licensed distributors) who distribute electricity generated by an offshore generating station by means of a distribution system which is not used to convey electricity generated otherwise than by offshore generating stations. It therefore covers only distribution systems which are conveying electricity generated offshore. At the stage where the distribution system also conveys electricity generated onshore, or where a licensed distributor operates the distribution system, the exemption will cease to apply. The exemption is subject to conditions set out in the Order.

Implications for onshore generators with similar connections

- 3.7 Two respondents, AMEC and Tony Cotton, argued that if Government policy is to require licences (or an exemption) for collection systems downstream of the metering point, then this should also apply to all onshore wind farms, other generating stations and industrial sites. The respondents considered this to be inappropriate or potentially discriminatory.

Government Response

- 3.8 The purpose of this consultation and the proposal to amend the exemption Order is to address a specific issue related to offshore distribution. This exemption will be an addition to the existing licensing and exemption regime and does not affect the continued application of the existing legislative framework. Those distributing onshore currently require a licence or an exemption. They will need to take their own legal advice on whether the existing class exemptions are applicable.

Incorporation of offshore distribution into the offshore transmission regime

- 3.9 A respondent agreed with the DTI that the regulatory regime for offshore distribution should be kept under review as these networks may develop over time. In addition, they considered that when there is further clarity on the arrangements for offshore transmission that we may wish to consider incorporating the offshore distribution regime in the regulatory regime for offshore transmission.

Government response

- 3.10 The Government believes the class exemption is capable of enduring and is flexible enough to provide for future build, although this will be kept under review as the offshore low voltage network develops. Should the make-up of offshore distribution systems change significantly, for example, should the offshore situation deliver a meshed network of connections or consumer demand be directly connected to these systems, then the impact on the security of the system might require further conditions to be attached to the exemption or possibly the creation of an offshore distribution licensing regime.

Application of the class D exemption to systems at 132kV

- 3.11 Another respondent, Warwick Energy, asked for confirmation that the class exemption would apply to 132kV connections until the enduring transmission regime is in place.

Government response

- 3.12 As stated in the consultation document, any person operating a 132kV connection (in England and Wales) who falls within the scope of the exemption pre-commencement of the relevant 2004 Act provisions would benefit from the exemption until the new definition of high voltage line in section 180 is substituted.

Correction of inaccuracies

- 3.13 The Government has also noted from responses that the planned connections of two projects were inaccurately reported in the consultation document. Rhyl Flats will connect at 33kV (not at 132kV) and Robin Rigg will connect at 132kV (not at 33kV).

ANNEX A : LIST OF RESPONDENTS

AMEC
BWEA
Centrica
EDF Energy
EMEC
energywatch
Eon
NGET
RWE Npower
SCIRA Offshore Energy
Scottish Power Energy Networks
SSE
SWRDA
Tony Cotton
United Utilities
Warwick Energy

