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Our ref: JCPT/12528/dk

Dear Sir

IEG Electricity Licence

We are in receipt of the 'Notice of a Proposed Decision to grant a Licence' and the 'Draft Licence issued to IEG Ltd under section 2(1) of the Electricity (Guernsey) Law, 2001' which proposes to grant to the Licensee a Licence to ***generate electricity for the purpose of giving a supply to any premises or enabling a supply to be so given***.

We remain of the view that the one week period given to make representations on such a significant market development is unreasonably short. We have already registered this concern with you. However, we note your decision to maintain the timetable for responses.

Given the potential major changes in market dynamics associated with this application a reasonable period of review in our view remains entirely necessary based on the issues and questions raised below. We therefore continue to suggest that serious consideration should be given to carrying out a wider consultation on the possible impacts and potential unintended consequences before granting a generation licence.

We reserve all our rights in this respect if you proceed with such a important decision notwithstanding the contents of this letter.

Introduction

Guernsey Electricity Limited (GEL) holds licences to generate, convey and supply electricity. We are bound by the conditions of those licences. In addition, we are also guided by governmental strategic policy and direction on the security of electricity supply to the island, energy policy and specific environmental direction. These obligations have been implemented within GEL in such a way so as to meet the interests and needs of all our customers fairly whilst ensuring the States of Guernsey achieve their strategic aims and objectives. The profitability of the business is therefore aligned to its role as an environmental enabler for the transition to a low carbon island by 2050. All profits made by the company are retained within the island for the benefit of the island.

The generation licence and the existing supply exemption proposed for IEG creates significant uncertainty and conflicts when considering the directions and policies that GEL is bound by. In our extremely small local market this raises fundamental questions of fairness across the different customer groups and market segments. For example, an early question will be who should pay for the infrastructure required by GEL in accordance with its existing supply licence obligations to back up IEG generators.

We have set out below our initial concerns and observations in relation to the granting of a licence to generate electricity for the purpose of giving a supply to any premises or enabling a supply. However, at the outset we should record that we are not, in principle, opposed to competition in the generation market or in fact the ability of customers to become "prosumers" whereby they produce and consume electricity. That said our principal overarching concern in this regard from a customer perspective is that any competition should be fair and equitable to all customers and does not create groups that benefit to the detriment of others.

In addition to the above cost recovery fairness matter, we also believe that the journey to reach the Island's low carbon aspirations needs to be considered in a wider context. Decisions made for a short term benefit of specific customer groups should not result in unintended consequences compromising the longer term strategic objectives of the Island. We are of the view that the granting of any further generation licences should be done whilst remaining cognisant of the direction dictated by the States of Guernsey through the Island's Energy Resource Plan (2012), the Guernsey Electricity Security of Supply (2014), and the various environmental legislation requirements, such as the The Environmental Pollution (Guernsey) Law, 2004.

We are particularly concerned with how the granting of a generation licence to IEG could prejudice alignment with, and achievement of, the objectives contained within these agreed States of Guernsey policies and directions.

We are also very aware that the Guernsey regulatory environment and structure was conceived and established well over 15 years ago and that considerable change has occurred in the Islands environmental aspirations, energy markets and political structures in the intervening period. It is imperative that these changes are also considered prior to the granting of further generation licences (under the existing arrangements) which will have a fundamental impact on the Guernsey electricity market and the States' environmental policies.

We will expand on these points below within the time allowed for a response. However, as raised above we do not consider we have had sufficient time to fully engage with all the related parties and stakeholders of GEL who will be affected and will similarly need to consider the application.

Energy Policy and Environmental Legislation

GEL, alongside our joint venture partners Jersey Electricity have, through significant investment in the Channel Islands Electricity Grid, allowed Guernsey to see significant reduction in the carbon intensity of electricity used on the Island. The Energy Resource Plan approved by the States of Guernsey in 2012 sets out very clearly this direction in terms of the carbon intensity of electricity generation. The two key extracts below highlight the direction given:-

- Clause 10.2 covers the energy vision for 2020 whereby: ***'there will be a gradual decarbonisation of Guernsey's electricity generation...'***
- ***Objective 3: reducing the environmental impacts of our energy consumption as part of our contribution to international initiatives as a member of the global community..... 'We will reduce the carbon dioxide emissions of each unit of grid supplied electricity and publish our achievements on an annual basis'***

In recognition of the above directions we are fully supportive of the introduction of renewable and low carbon distributed generation on the island. This support is subject to the implementation being facilitated in a fair and equitable way. However, we question whether introducing further hydrocarbon generation of electricity onto the system aligns with the above strategic policy direction for carbon reduction; this would be the consequence of granting the proposed licence. Whilst we accept that the use of combined heat and power in other jurisdictions with much higher delivered electricity carbon intensities (UK grid intensity is 430 gCO²eq/kWh) may be an appropriate measure to reduce the grid intensity, the current position in Guernsey is very different. GEL imports electricity having a carbon intensity of 4 gCO²eq/kWh for nuclear and 6 gCO²eq/kWh for hydroelectricity. When this is combined with the need to generate a small amount of electricity locally in the near future, we can achieve the option to supply delivered electricity at 61 gCO²eq/kWh, this being the current maximum importation level. (In 2016/17 the actual carbon intensity for Guernsey Electricity was 138 gCO²eq/kWh, which represented the conveyance least cost dispatch requirement combined with works on the CIEG network). The net effect is that GEL supplies electricity with a significantly lower carbon intensity than the UK. We are unaware of the carbon intensity of the specific technology which IEG intends to employ, but we would caution that any claims made as to its environmental benefits are likely to be derived from comparison to the UK or a similarly high carbon intensity grid.

Whilst, absent any specific Government direction, this may not be a factor which the Guernsey Competition and Regulatory Authority is required to consider in its decision to grant or refuse a licence, we are strongly of the view that a longer and wider consultation with the relevant parties, particularly the Committee for Environment and Infrastructure, would allow them to consider whether a specific strategic policy direction should be given to the Authority. In any event it must be a material consideration.

Market and Investment Dynamics

As an owner of generation, conveyance and supply assets with the associated licences, GEL has been obliged to provide sufficient security for all Island electricity supplies. Long-term, 25 year investment plans have been developed to ensure appropriate provision for all of the Island's needs in this respect.

It is unclear from the very limited information published to date how IEG intends to operate their generation plant under the proposed licence application. In the absence of such detail it is not possible to fully consider the ramifications and impact on the above requirements or other electricity customers.

It is unclear what new obligations would fall on GEL as the sole Conveyance and Supply Licensee (and therefore the supplier of last resort, when the distributed generation is not available) as a result of this application. The entity or persons responsible for the costs for maintaining GEL as the supplier of last resort when the IEG distributed generation is not available (as per the requirements of Section 10 of the Electricity Law) has not, to GEL's knowledge, been specified. There are cost recovery arrangements in place for current customers who self-generate and require the back up of an electricity network connection for times when they choose not to generate or are unable to generate. However, we require clarity on how the GCRA would allow for the recovery of the costs associated with this provision for IEG's customers so as not to disadvantage GEL's remaining customers? This should include how the GCRA intends for GEL to be compensated for the investment it has already committed to avoid the risk of stranded assets due to insufficient returns on previous capital expenditure.

The result of any significant reduction of the recovery of costs for GEL would be to introduce unfairness into the electricity market, as those costs would have to be recovered from fewer customers leading to an increase in their electricity charges. Customers of GEL would be subsidising IEG customers in terms of infrastructure and back-up. IEG cannot be permitted to cherry-pick the market to create a privileged group of consumers making short-term savings on their personal electricity bills whilst compromising the island-wide plan, not contributing to the cost of securing a back-up supply for themselves, and all the time using a technology which is in all probability more polluting than the GEL offering.

Another unintended consequence of the grant of a generation licence to IEG (alongside the existing supply exemptions) will be the loss of policy coherence for future energy policy direction. The inability for Government to manage energy transition investment may result in the island not achieving its environmental and security objectives and targets. The potential loss of control of demand on the electricity network would also impact GEL's infrastructure investment decisions, and adversely affect GEL's ability to meet the obligations within the energy resource plan and electricity security of supply requirements. For example, GEL is currently obliged to provide an N-2 security of electricity supply standard and plan for a second subsea connection to the island. The island's ability to make further use of low carbon nuclear energy depends on GEL's ability to meet those obligations, and its ability to do so would be severely affected by a change in the market dynamics.

In order for GEL and other respondents to properly consider the consequences, it would be helpful if the GCRA would release the relevant parts of IEG's generation licence application and associated supporting documentation so that we can assess these impacts and how we ensure the potential to disrupt the electricity market in a negative way is avoided, or managed appropriately.

Customer supply and protection

Another matter we believe we need to raise in relation to the IEG generation licence is the existing exemption from the need to have a supply licence.

We believe that the exemption of IEG from the need for a supply licence does not appear to take into account customers interests in terms of pricing, quality of service levels, permanence and variety of utility service given that IEG intends to supply potentially multiple customers on a commercial basis in competition with GEL.

GEL as a licensed supplier, has a strict regulatory obligation as to these matters and so, therefore, should IEG by way of being licensed for supply to customers with appropriate licence conditions equivalent to those imposed on GEL. GCRA's apparent acceptance of IEG being exempt from the need for a supply Licence, either in the form of a Public Electricity Supply Licence (given the intention for IEG to supply island wide) or a more limited Special Supply Licence as defined in the Electricity Law, has the potential to create an issue in terms of the above customer interests for an increasing number of IEG supplied electricity customers in the future. In addition, the existing exemption from the need to apply for a supply licence leads to the creation of two supply markets where the two competing parties have different obligations to supply an essential service.

We would question therefore how, under these circumstances, the GCRA intends to fulfil its duty, particularly in respect of quality and service to consumers, under section 2(a) of the Regulatory Law to protect the interests of potential customers of IEG. It is GEL's view that a requirement placed on IEG to hold a supply licence containing appropriate conditions would enable GEL and IEG to compete on a more balanced and equitable basis; although this does not address the concerns expressed earlier in this letter.

As stated throughout this response we believe that further, more detailed, consideration needs to be given to the application, particularly in respect of the exemption from a supply licence. We would ask for clarification as to conditions which must be met before a supply licence is required and thus how many customers could potentially be adversely affected by an unregulated entity providing an electricity supply.

Regulatory Environment

Finally, the GCRA will be aware of the States of Guernsey's intentions as regards the regulatory environment. The GCRA will also be aware of the intended implementation of the required legislative changes to bring this new regime into force. The States approved and directed, in the joint proposals from the Commerce and Employment Department and the Treasury and Resources Department, the Alternative framework for the oversight of Guernsey Electricity Limited and Guernsey Post Limited (Billet d'Etat VI of 2015, Resolution III). It will also be aware of the direction to prepare such legislation as may be necessary to give effect to the decisions made on the 18th February 2016. The legislative changes have been prepared based on the current market position whereby GEL is the only licensee for generation, conveyance and supply. The proposed license is inconsistent with the direction already set by the States and would cause considerable disruption. Again this is a reason for longer and wider consultation as to the consequences of granting a licence at odds with the will of the Island's parliament as regards energy policy, the environment and regulation.

Summary

This application for a licence therefore raises many fundamental questions as to the nature of the funding of the Island's electricity system, the regulatory environment and the delivery of the environmental aspirations of the island in circumstances where the States of Deliberation and the Island's government have already expressed their wishes. We would therefore strongly recommend that before issuing a licence to generate electricity for the purpose of giving a supply to any premises or enabling a supply to be so given, the GCRA consider the issues and questions raised in this response and hold a wider consultation to understand and fully consider the consequences of any such licence being granted.

We would be pleased to take part in a detailed technical and legal review with GCRA to discuss the implications, whether intended or unforeseen, as soon as possible.

We therefore request that the licence is not granted until there has been a much longer consultation to carefully consider the above issues. We are very happy to cooperate with the regulator in this respect but, equally, must reserve all our rights to challenge the shortness of the notice given of this proposed decision as well as the decision itself, should you proceed, notwithstanding, to grant the proposed licence.

Yours Sincerely



JULIAN P TURNER
Chief Financial Officer