



Standby Charge for Embedded Electricity Generation

Call for Information

Channel Islands Competition & Regulatory Authorities

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1. Introduction

- 1.1 In August 2017, CICRA granted an electricity generation licence to International Energy Group Limited (**IEG**) to *'generate electricity for the purposes of giving a supply to any person or enabling a supply to be given'*. This was the first such licence granted to a competitor to Guernsey Electricity Limited (**GEL**) in the electricity market in Guernsey.
- 1.2 IEG has expressed interest in supplying potential customers through the installation of Combined Heat and Power (**CHP**) at its premises and has been in discussion with potential customers for some time.
- 1.3 A key component in the decision making of potential customers in whether to take such supply from IEG is the total cost to the customer of their electricity supply. This includes the cost of supply from IEG but also the standby charge imposed by GEL. The standby charge is a monthly charge levied by GEL for installed capacity to customers with embedded generation capacity exceeding 25kW. This charge is currently set by GEL at £6.8594 per kW.
- 1.4 It is understood that GEL views the application of a standby charge as being appropriate where it remains necessary for GEL to continue to provide backup electricity supply to a premises which has an alternative embedded generation capacity. GEL believes it necessary to recover the cost of this backup supply but should a customer disconnect permanently from the GEL network then no such charge would apply.
- 1.5 GEL has also indicated, in correspondence with IEG, that it is undertaking a detailed review of its charging and tariff structure with a view to revising certain of its charges to reflect direct and variable costs. In its view this will include consideration of the application of the standby charge.
- 1.6 IEG has requested that CICRA reviews the application of the standby charge by GEL as it is IEG's view the charge is an abuse of GEL's dominant position in the electricity supply market and that by imposing a standby charge GEL is engaging in practices or entering into arrangements which have the object or likely effect of preventing, restricting or distorting competition in breach of its licence.
- 1.7 CICRA is aware that the issue of standby charges for such embedded generation capacity is currently the subject of review in Jersey following a debate in the States of Jersey on the application of a standby charge by Jersey Electricity (**JEC**). In light of this review JEC voluntarily agreed to defer application of the charge – currently set at £3.10 per Kw (excluding GST) for installations up to 50kW - pending the outcome of this review. The review is being carried out by Jersey's Environment Department.
- 1.8 The principle of the application of a standby charge by GEL has not been examined in Guernsey previously. With the advent of competition in the electricity supply market the imposition of the charge raises questions that appear to CICRA to warrant fuller consideration. These include whether the application of such a charge is in the best interest of all electricity customers in Guernsey and, if so, whether the level of the charge is appropriate.

- 1.9 CICRA is aware, from confidential information provided to it, that IEG is in discussions with potential customers and that clarification of the principle of the charge and level - if determined that one should be applied - are material considerations for its potential customers. Therefore CICRA is now seeking views of interested parties to inform its further consideration of these issues. CICRA has been provided with confidential information by IEG on its estimate of the likely loss of revenue to GEL should it not be able to levy a standby charge pending the conclusion of this review. CICRA is considering, given the limited materiality to GEL of this potential lost revenue, whether to direct that the standby charge be waived by GEL pending resolution of the issue. This mirrors the approach adopted voluntarily by JEC in Jersey.
- 1.10 CICRA is conscious that one possible outcome from this review is that a standby charge is appropriate for the Guernsey market. It is important that a balance is achieved between GEL's commercial interests and those of any other parties who may be impacted by this review. Therefore CICRA believes it is important that as part of this review, should it be concluded that a standby charge is appropriate, and if so once the level of the standby charge has been determined, that there is an undertaking from parties liable for any charge to pay the determined amount to GEL. It is also important that any outcome is fair to all users of the electricity network in Guernsey and that unfair or anti-competitive cross subsidies be avoided.
- 1.11 CICRA welcomes your views and evidence on the discussion points raised in this consultation and in particular on the specific questions set out later in this paper.

2. Embedded Generation – Background

- 2.1 The concept of embedded generation – sometimes referred to as distributed generation – has been around for sometime and is common in other markets. However, it is only in more recent times that rollout of such generation has become an issue of interest in Guernsey and has necessitated the need by CICRA, and the market, to examine in greater detail the merits of a standby charge.
- 2.2 While IEG’s current interest is in CHP type installations, CICRA believes that as part of this review the principles that should apply, and charges, if any, that are ultimately determined, should lend themselves to any form of embedded generation, including renewable generation.
- 2.3 In broad terms the logic for a standby charge (or insurance charge as it is sometimes referred to) is that, in circumstances where a customer (generally large commercial customers) has an alternative supply to that from the main network (in Guernsey’s case the GEL main network) it may be necessary for the customer to remain connected to the main network in case of disruption to its own, on-site supply source. This ‘back-up’ enables a customer to have certainty on its electricity supply.
- 2.4 The nature of disruption may come from three main categories and each raises different issues for the duration and form of back-up need. The three main categories are; where there is planned maintenance to the on-site supply; unplanned maintenance; and supplemental service. In more detail these are:
 - 2.5 Planned Maintenance – this is where the customer sited generation capacity is scheduled to be offline for a period. In theory, such planned maintenance can be arranged to occur at times with minimum impact on the main generator, i.e. at off-peak demand times, and may result in fewer if any additional costs to the main generator.
 - 2.6 Unplanned maintenance – this is essentially where the on-site generation is unavailable and the customer relies on the main generator for its supply while service on-site is restored. As is clear, such unplanned outages require the customer to rely on the main generator at short notice.
 - 2.7 Supplemental service – in circumstances where it is already known that the on-site generation capacity can’t meet all - or at certain times none – of the customer’s demand needs, the customer relies on the main generator.
- 2.8 Focusing on the Guernsey context, it is clear that even in circumstances where a customer chooses to self-generate, there will, in most cases, remain a need for an on-going relationship with GEL. While a customer may choose to disconnect permanently from the GEL network, for the reasons outlined above, the likelihood is that most self-generating customers will continue to opt for a connection to GEL. Therefore GEL will need to maintain infrastructure to the customer’s premises and retain the ability to bill on an on-going basis. This is apart from any technical or safety elements of the relationship that will need to be ensured.

- 2.9 However, it is also clear that the revenue to GEL from such customers will be less than prior to their decision to self-generate. A self-generating customer will only need to purchase electricity for its needs in circumstances where its on-site supply is unavailable for whatever reason. Such self-generation therefore has potential implications for how GEL funds its wider capital investment. The capital investment needs of GEL, in circumstances where there are only a limited number of embedded generation sources, may likely be only marginally different, if at all, to a scenario where GEL generates all electricity for all customers.
- 2.10 There may however be benefits from embedded generation that Guernsey as an economy may wish to exploit. These include reduced line losses as the generation takes place on-site, potentially cheaper electricity for the customer, an available source of backup in the event that GEL's generation capacity is unavailable. There may also, depending on scale of self generation, be an opportunity for the customer to sell electricity back to the grid (subject to agreement with GEL being negotiated). These are all matters that may be relevant to the States of Guernsey as it formulates its energy policy.
- 2.11 This current consultation is aimed at addressing a complaint made by IEG about the application of a standby charge by GEL. IEG alleges that the application of a standby charge by GEL is an abuse of its dominant position in contravention of general competition law¹ in Guernsey and that by imposing the charge, GEL is engaging in practices or entering into arrangements which have the object or likely effect of preventing, restricting or distorting competition which it claims is a breach of condition 13 of GEL's electricity licence.
- 2.12 In respect of the abuse of dominance allegation, IEG has offered a number of reasons why it believes GEL may be in breach of its legal obligations. These include
- that the charge applied by GEL, in its view, appears to bear no relationship to the costs it purports to cover;
 - that GEL is imposing a charge on potential customers of a competitor that it does not apply to its own customers;
 - that the charge discriminates between customers who choose to supplement their energy options with electricity and other energy sources; and
 - that the charge acts as a deterrent to customers considering purchasing their energy needs from a competitor of GEL by raising the overall cost of their energy needs potentially making the switch to a competitor uneconomical.
- 2.13 IEG also highlights that the charge applied by GEL (£6.8594 per kW) is over twice the charge applied in Jersey by Jersey Electricity (£3.10 per Kw (excluding GST)) and notes that even this charge in Jersey is now subject to review by the States of Jersey following concerns raised there. Further it believes GEL should recognise the benefit embedded generation has for the island by reducing peak demand.

¹ <http://www.guernseylegalresources.gg/CHttpHandler.ashx?id=77021&p=0>

3. CICRA's consideration of these issues

- 3.1 Ensuring the energy market in Guernsey works well for all parties – consumers, providers and the wider island economy and environment – are key considerations for CICRA. In terms of consumers, CICRA would wish to see consumers' benefit from a fair price for their energy needs and have access to choice, where that is available to them. With respect to providers, CICRA is very aware of the need for providers to be able to invest to ensure the provision of a robust, efficient supply of energy. For GEL in particular, it is subject to specific States guidance in respect of security of supply that means it must keep generation capacity (either on-island or through its interconnector with France) to meet the States' requirements. For the wider Island economy, the provision of economically priced energy helps contribute to Guernsey being a cost-competitive jurisdiction for business. For the Island's environment, CICRA would wish to ensure that the regulatory regime for the wider energy market is such that it promotes an approach that supports the States of Guernsey's energy policy and does not negatively impact on any changes to the policy which may be brought forward by the Committee for Environment and Infrastructure in the future.
- 3.2 The current standby charge, which has been set by GEL, has not been subject to any specific review and CICRA is aware that GEL has indicated that it is currently planning to review the structure of this and other tariffs this and other charges. No timeline has been provided for this review, nor is it clear what approach GEL intends to adopt towards such a review.
- 3.3 The last review by CICRA of GEL's tariffs was in 2012. That review – and indeed earlier reviews – did not focus on structure of every tariff, as such an approach, at that time, would not have been proportionate. CICRA is conscious that a wholesale review of every GEL tariff will require significant resources to be deployed by both GEL and CICRA. CICRA is mindful of the decision by the States of Guernsey to amend the regulatory regime in Guernsey for the regulation of GEL. While this has not been finalised – and for now GEL remains subject to all of its regulatory obligations – the complaint raised by IEG would still fall to be considered by CICRA under general competition law.
- 3.4 With this in mind, CICRA for now is seeking views on how best to address the issues raised in a timely, proportionate and constructive manner. In undertaking this assessment, CICRA will seek to assess what charge if any is appropriate bearing in mind the following key principles. It will seek to ensure that any charge is
- Fair
 - Does not distort the market and
 - Is proportional and practical
- 3.5 In considering fairness, CICRA is mindful that, when setting or amending any tariff, there is always a risk for there to be winners and losers. In this case, where GEL is required to fund its capex through the recovery of costs from tariffs any change to one tariff or charge which reduces income may mean, all things being equal, that tariffs elsewhere may need to rise. CICRA would wish to ensure that in assessing the standby charge, its assessment takes account of the costs to GEL of maintaining a connection to a customer who chooses to self-

generate along with any benefits that might arise to GEL from having embedded generation available to reduce peak demand.

- 3.6 A further key consideration for CICRA is ensuring that investment in infrastructure in the wider energy market is sustainable. A standby charge that is set at a level higher than justified may result in competitors to GEL exiting the market, in this case IEG abandoning the development of CHP projects with potential customers. It would also result in GEL being over compensated for the actual costs it incurs in providing a standby service to customers. A standby charge set too low (or zero) may result in inefficient investment that effectively sees an over development of embedded generation that is unsustainable longer term. GEL may also not fully recover its justified costs, with the result that other customers effectively cross-subsidise the provision of standby service to potentially large self-generating customers. In circumstances where CICRA is mindful that electricity bills may be one of the large bills for households, in particular vulnerable households, avoiding such a scenario is a key consideration.
- 3.7 Finally, CICRA is aware from previous work in reviewing GEL tariffs that such an undertaking will generate resource requirements for all involved. Such a review will require GEL to set out the rationale and basis for the charge in a manner that is transparent and supports its justification for the charge. Other interested parties, and IEG in particular, will need to engage constructively in assisting in reviewing this charge. There will also clearly be a significant resource requirement from CICRA.
- 3.8 CICRA is also mindful of the risks of looking at any one tariff in isolation given the distortionary risks outlined above. In considering how best to assess this charge, CICRA is keen to ensure the proportionality of any review. Achieving a review in a proportionate manner obviously requires a partnership approach from all involved.

Question 1: Does the respondent agree with CICRA's proposed principles for reviewing the GEL standby charge? If the respondent has alternative views or relevant evidence, the respondent is asked to explain those and provide all of its analysis and assessment relating to this matter to inform CICRA's consideration and next steps.

4. Standby Charge – Proposed Approach

- 4.1 As noted above, the issue of a standby charge raises a number of competing interests and there is likely to be a need to balance those competing demands in achieving an outcome that is in the best interests of the market as a whole. Included among these are
- the needs of the customers looking to take advantage of embedded generation by seeking to reduce their overall energy costs;
 - the interests of competitors to GEL who are keen to gain entry to this market;
 - GEL as the main provider of the island’s electricity infrastructure;
 - existing electricity customers who may be impacted by increased electricity bills by any reduction in contribution from larger customers; and
 - the States of Guernsey who have responsibility for energy policy.
- 4.2 As noted earlier, Jersey is currently reviewing the standby charge applied by JEC following a debate on the issue in the States of Jersey earlier this year. The States of Jersey’s Council of Ministers agreed to a review noting:
- “Although minimal currently, the number and scale of embedded renewable energy generators could grow at a significant rate. Without charging the embedded generators the true cost of ‘standby’, inequality is caused with non-generators potentially subsidising generation and non-generators being asked to bear an increased burden of fixed costs.”²*
- 4.3 Similar considerations will need to be assessed in Guernsey. JEC is not subject to regulation and Jersey’s Environment Department is undertaking the review referred to above. CICRA intends to take account of that review once publicly available to inform its own further consideration of this matter.
- 4.4 While the States of Guernsey has determined to remove GEL from regulation at some future point, currently it remains subject to the provisions of the electricity law and its licence conditions. Of particular relevance to this issue is GEL’s licence conditions 13 (Fair Competition) and Condition 20 (Price Regulated Services). In the past CICRA has undertaken a careful overall assessments of revenue from tariffs GEL has looked to change, although since 2012 no such detailed review has taken place – this reflects the guidance from the States of Guernsey on the proportionality of regulation for the electricity sector and on GEL in particular.
- 4.5 In order to come to a view on the fairness or otherwise of GEL’s standby charge, there may be a need to undertake a more detailed assessment of the rationale for the charge, its cost-justification and the implications any change to this charge may have for other tariffs. Therefore CICRA is interested in exploring all possible mechanism for determining an appropriate level of charge in a manner that is proportionate and cost-effective to all concerned.

² <https://statesassembly.gov.je/assemblypropositions/2017/p.88-2017com.pdf>

- 4.6 One possible approach is to benchmark the charge against other providers of similar services. As noted earlier, JEC provides a similar service at a cost approximately 50% less than GEL's current charge. While useful to know, without a better understanding of how the charge is composed and how it relates to other tariffs JEC may charge, CICRA is not prepared as this time to accept it as benchmark. CICRA also notes that there are concerns about the charge and it is subject to review at this time. In response to Question 2 below CICRA would welcome views on whether benchmarking may provide an acceptable proxy for determining GEL's standby charge and if so respondents' views on appropriate jurisdictions to benchmark GEL against would be welcome.
- 4.7 A further option is to undertake a review of GEL's justification for the charge to understand what costs are recovered through the charge and how it relates to other tariffs GEL currently charges. While this has an obvious benefit of being focused specifically on the circumstances that exist in Guernsey, any such review will only be as good as the data it is based on. For such reviews, regulators have tended to look to detailed regulatory accounts for sufficient granularity of the costs that go into arriving at the justification for the charge.
- 4.8 GEL has not updated its regulatory accounts for some time and CICRA is mindful that to do so for a review of one specific tariff may not be appropriate. It would likely take a significant amount of time before such accounts would be in a form that would enable CICRA to rely upon them for making tariff decisions. During this time neither GEL, IEG nor the market would have certainty on the level of charge that may result in investment decisions being made without full certainty. On the other hand, allowing a charge which is also not cost justified remain at its current level may result in a dampening down of demand.
- 4.9 As the potential number of customers that CICRA is aware of that are actively interested in availing of embedded generation is low, CICRA is minded to set the standby charge to zero pending the outcome of this review. The materiality of any forgone revenue to GEL is likely to be low during the duration of this review whereas retaining it at its current level may inhibit future market development.
- 4.10 CICRA is conscious that any charge that is ultimately determines may equally inhibit demand for embedded generation. It would wish it to be understood and accepted by those providing and availing of embedded generation that they carry risks in proceeding with developments and would be liable for any charges subsequently determined by CICRA and retrospectively applied.

Question 2: Does the respondent agree with CICRA's proposal to set the standby charge applied by GEL at zero pending the review of the charge? If the respondent has alternative views or evidence, including suggestions on benchmarking, the respondent is asked to explain those and provide all of its analysis and assessment relating to this matter to inform CICRA's consideration and next steps.

6. Next Steps

- 6.1 CICRA is seeking views on the matters covered by this consultation to further inform its consideration of the issues raised.
- 6.2 Interested parties are invited to submit comments to CICRA in writing or by email on the matters set out in this document to the following addresses:

2nd Floor, Salisbury House 1-9 Union Street St Helier Jersey JE2 3RF Email: info@icra.je	Suite 4, 1st Floor La Plaiderie Chambers La Plaiderie St Peter Port Guernsey GY1 1WG Email: info@icra.gg
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- 6.3 All comments should be clearly marked 'Standby Charge for Embedded Electricity Generation' and should arrive by 5pm on 8 August 2018.
- 6.4 In line with CICRA's consultation policy, it intends to make responses to the consultation available on the CICRA website. Any material that is confidential should be put in a separate annex and clearly marked as such so that it may be kept confidential.

END.