

electricitynetworkcharging@ofgem.gov.uk

National Grid ESO
Faraday House
Gallows Hill
Warwick
CV34 6DA

Camille.Gilsenan@nationalgrideso.com

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ESO Response to Ofgem's Open letter on regulatory arrangements for independent distribution network operators

Dear Network Charging Team,

Thank you for the opportunity to respond to your Open Letter on Regulatory Arrangements for Independent Distribution Network Operators.

Who we are

As the Electricity System Operator (ESO) for Great Britain, we are at the heart of the energy system, balancing electricity supply and demand second by second.

Our mission, as the UK moves towards its 2050 net zero target, is to drive the transformation to a fully decarbonised electricity system by 2035, one which is reliable, affordable, and fair for all. We play a central role in driving Great Britain's path to net zero and use our unique perspective and independent position to facilitate network and market-based solutions to the challenges posed by the trilemma.

Our transformation to a Future System Operator (FSO) is set to build on the ESO's position at the heart of the energy industry, acting as an enabler for greater industry collaboration and alignment. This will unlock value for current and future consumers through more effective strategic planning, management, and coordination across the whole energy system.

Our key points

The ESO strongly supports competition and believes that in the area of connections it can be an important part of the solution to facilitating quicker network connections for new users. We are supportive of independent distribution network operators (IDNOs) and understand that their original purpose accorded with Ofgem's original stated vision for them: *"to serve new housing developments on both greenfield and brownfield sites"*. We have seen this now start to evolve, including from our viewpoint, direct connections to the transmission system and as such welcome this review. We have summarised our key points below and provided further detail in Appendix 1.

- **We support any arrangement which increases the speed for customers to be connected to the network in an efficient and economic manner whilst maintaining a safe and resilient network.**

Any arrangement which reduces the connections queue should be encouraged, within arrangements that ensure the long-term planning and development of a safe, secure and economic network. The current licence obligations on IDNOs are lower than those applied to DNOs due to the restricted nature of the IDNO network originally envisioned. As the IDNO networks evolve in purpose (LDNOs as referred to in the open letter) and increase in size and complexity, the licence should ensure appropriate treatment reflective of this to prevent a 2 tier connections process.

- **Consideration is needed to ensure efficient co-ordination between an increasing number of parties especially given the increasing co-ordination between ESO and DSOs.**

There is a long-expressed aim to move towards greater DSO-ESO co-ordination in the longer term, though the path to get there is not yet entirely clear. It would therefore be helpful to clarify the role of these LDNOs in that

process. The pathway may include extending the ability to influence the output of generators, down to smaller Distributed Generation than at present. Clear licence obligations will be required to ensure data and access is easily available to the relevant system operator. As noted, it is also paramount that existing standards and requirements are satisfied irrespective of whether a customer connects to a DNO's system or IDNO's system.

- **The charging regime needs to be suitable for any new proposed arrangements to ensure everyone pays their fair share for the network.**

There are current charging arrangements which allow the IDNOs to offer discounted connection rates due to the lower requirements of smaller networks and so consideration needs to be given to ensure any charges are fair in the long-term considering the increase in network size and the associated cost of maintaining a resilient network. As the number of these networks and the EHV connections to these increase we agree there is a need for transparency and regulation around the charging arrangements that are to apply.

We look forward to engaging with you further. Should you require further information on any of the points raised in our response please contact Camille Gilsenan, Commercial Codes Change Manager: Camille.Gilsenan@nationalgrideso.com .

Yours sincerely

Jamie Webb

Head of Market Frameworks

National Grid ESO

Appendix 1 Consultation Question Responses

Question 1: What do you consider to be the pros/cons of IDNOs connecting EHV customers embedded within distribution networks?

Pros

- Competition in connections encourages innovation, investment and challenges the status quo approach.
- Connecting EHV customers within LDNOs which could directly be connected to the transmission network would remove additional interfaces, and potentially network constraints, which may allow a greater ability to access renewable generation and also provide ancillary services to the ESO.
- IDNOs can discount via an Asset Adoption Value payment which cannot be offered by DNOs thus providing a potentially cheaper connection to customers.
- IDNOs may be able to invest in/build new network more quickly than a DNO.

Cons

- It is not clear if there is any consideration for futureproofing of the network to ensure the network is developed in the most economic and efficient way in the long term.
- With a significant increase in the volume of iDNOs, there would need to be enhanced co-ordination between parties to ensure there is the capability, resource, and expertise to contribute to the operation and planning of the network such as System Restoration and facilitate Distribution Restoration Zones
- There is an aim to move towards greater DSO-ESO co-ordination in the longer term. How IDNO assets fit into this needs to be considered.
- There have been iDNO failures which have left assets stranded. They have a lower financial threshold to enter the market so any further expansion will need to consider adequate financial security provisions without creating unnecessary barriers to entry.
- EHV customers would need to be subject to the same requirements and standards as those connected to DNOs.
- It is not clear if there is any consideration for futureproofing of the network to ensure the network is developed in the most economic and efficient way in the long term. There have been concerns that we have seen an increase in parties seeking to move their directly connected (transmission) BCA agreements across to embedded agreements on the encouragement of iDNOs, which is a different behaviour to that which we see at a DNO level.
- We understand that it was envisaged that iDNO arrangements would be extensions of DNO networks, however, we have seen examples where this is not the case. Therefore, unintended consequences need to be considered.

Question 2: What do you consider to be the pros/cons of IDNOs connecting directly to the transmission network?

Pros

- It may offer alternative innovative connections to customers which are quicker to connect and more economical due to not needing to reinforce the wider distribution network.
- IDNOs can discount via an Asset Adoption Value payment which cannot be offered by DNOs thus providing a potentially cheaper connection to customers.
- IDNOs may be able to build new network more quickly than a DNO due to increased capacity of resource with additional parties.

Cons

- The requirements on completely new Distribution Networks are more onerous than those on existing or extended Distribution Networks due to the DCC regulations. It is not clear if an IDNO creating a new distribution system from a Transmission connection would be as economically efficient as a DNO extension.
- Charging arrangements would need to be appropriate and consistent with the general intent of Ofgem's targeted charging reform, in particular in the context of any self-supply exemption.
- There have been IDNO failures which have left assets stranded. They have a lower financial threshold to enter the market so any further expansion will need to consider adequate financial security provisions without creating unnecessary barriers to entry.
- It is not clear if there is any consideration for futureproofing of the network to ensure the network is developed in the most economic and efficient way in the long term. There have been concerns that we have seen an increase in parties seeking to move their transmission directly connected agreements across to embedded agreements on the encouragement of IDNOs, which is a different behaviour to that which we see at a DNO level.
- We understand that it was envisaged that IDNO arrangements would be extensions of DNO networks, however, we have seen examples where this is not the case. Therefore, unintended consequences need to be considered.