



Modification proposal:	DCUSA Change Proposal DCP066/DCP066A – Enhanced Provision of Cost Information		
Decision:	The Authority ¹ directs that DCP066A be made and DCP066 not be made ²		
Target audience:	DCUSA Panel, Parties to the DCUSA and other interested Parties		
Date of publication:	11 January 2011	Implementation Date:	26 January 2011

Background to the proposed modification

Suppliers and Independent Distribution Network Operators (IDNOs) need to be able to forecast their costs in order to plan various aspects of their business (pricing strategies, cash management, etc). A key input to these cost forecasts is the level of distribution use of system (UoS) charges made by Distribution Network Operators (DNOs). The calculation of UoS charges is particularly dependent on DNOs' allowed revenues, among other things. The DNOs are best placed to forecast their own allowed revenue, as they will have the best insight into their likely performance against price control incentive schemes and other operational aspects of the distribution price control.

DCP030 and DCP050 were approved and implemented on 26 February 2009 and 25 February 2010 respectively.³ DCP030 sought to provide detailed information Suppliers and IDNOs require in respect of DNOs' allowed revenue and expected changes to use of system charges. DCP030 introduced DCUSA Clause 35A which mandated DNOs to provide quarterly revenue information. DCP050 introduced a requirement on DNOs to host regular teleconferences to explain this information to interested parties. The transparent and regular provision of relevant information on revenues and forecast movement in charges ensured that all DCUSA Parties have access to common information about DNOs' revenues for forecasting of UoS charge changes.

However, it was considered that the reporting under Clause 35A does not allow users to see the assumptions DNOs make in arriving at their forecasts. As it stands, Suppliers and IDNOs are finding it difficult to fully assess the basis and consistency of the information, thus reducing its usefulness. DCP066 and DCP066A both seek to improve the quality of revenue information currently reported on a quarterly basis by DNOs.

The change proposal

DCP066 was proposed by British Gas to require the reporting of additional information to that provided under Clause 35A.

DCP066 aims to expand on the information already submitted under DCPs 030 and 050 by requiring the provision of additional information that would allow stakeholders:

- to improve their understanding of the link between revenues and use of system charges

¹ The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably in this document. Ofgem is the Office of the Gas and Electricity Markets Authority.

² This document is notice of the reasons for this decision as required by section 49A of the Electricity Act 1989.

³ Decision letters for DCP030 and 050 can be found on our website at <http://www.ofgem.gov.uk/Licensing/ElecCodes/DCUSA/Changes/Pages/Changespage.aspx>

- to improve their understanding of the forecast costs provided under DCP030 because more detail would be provided regarding the estimates
- to obtain more accurate forecast models and build stronger business plans.

The proposal would require DNOs to provide details of additional significant items in Table 1 of Schedule 15 of the DCUSA.⁴ According to the proposer, the information should allow users to track revenues from DNOs' Price Control settlements through the DNOs charging methodologies (eg the Common Distribution Charging Methodology (CDCM)) and into final UoS charges, with each significant element itemised.

The proposal would also introduce new requirements for DNOs to provide a range of possible values for volatile items contained within the revised Schedule 15 as Table 2. DNOs will have to provide details of Low, Central and High⁵ case values for t, t+1, t+2 for the items reported on in Table 2.

As a result of the consultation and subsequent request for information (RFI) responses, two variations were developed by the DCP066 working group – DCP066 represents the original proposal and DCP066A represents an alternative. Both variations require DNOs to submit the same information but they differ in the frequency and timing of their submissions.

Under DCP066 and 066A DNOs' would be required to report on the state of their revenue in relation to the current regulatory year, the last full regulatory year and the forthcoming four regulatory years. DCP066 and 066A vary in the frequency of reporting during the year. That is, DCP066 requires that Table 1 is reported on the fifth working day of each month and Table 2 is reported on the fifth day of April, July, October and January only. DCP066A requires that both Tables 1 and 2 are reported on the fifth working day of May, August, November and February.

DCUSA Parties' recommendation

The overall recommendation of DCUSA Parties in accordance with Clause 13.5 of the DCUSA is that DCP066A be accepted and DCP066 be rejected.

The DCUSA Parties also voted on a proposed date for these change proposals to become effective. Both DCP066 and DCP066A are intended to be implemented ten working days after a decision from the Authority to implement one or the other.

The majority of DNO and IDNO Parties voted to reject both the DCP066 solution and implementation date while the majority of Supplier Parties voted to accept it:

DCP066	Weighted Voting (%)					
	DNO		IDNO/OTSO		SUPPLIER	
	Accept	Reject	Accept	Reject	Accept	Reject
Change solution	9%	91%	0%	100%	58%	42%
Implementation date	37%	63%	33%	67%	58%	42%

⁴ For full details of the reporting requirements proposed by DCP066 and 066A, please visit the DCUSA website: <http://www.dcusa.co.uk/Extranet/CP.aspx?id=93>

⁵ The 'central' reported position (ie the mean) should be accompanied by an estimate of the 'low' case (ie the 10th percentile (P10)) and 'high' case (ie the 90th percentile (P90)) for the reported item.

There was much clearer support for the alternative proposal. A majority of DNO Parties supported the DCP066A solution and implementation date and all IDNO and Supplier Parties voted unanimously to accept the variation:

DCP066A	Weighted Voting (%)					
	DNO		IDNO		SUPPLIER	
	Accept	Reject	Accept	Reject	Accept	Reject
Change solution	83%	17%	100%	0%	100%	0%
Implementation date	83%	17%	100%	0%	100%	0%

Suppliers are intended to be the main beneficiaries of DCP066 and 066A. Whilst the votes identify a clearer preference for the alternative proposal, when asked which of the original and the alternative proposal were preferred by suppliers, the original proposal was the most popular.

The Authority's decision

In coming to a decision the Authority has evaluated the proposal against the DCUSA objectives⁶ and our wider statutory duties. We have also considered the views of DCUSA Parties that were raised in response to the DCUSA Panel's consultation and RFI and also the result of the vote by DCUSA Parties. We note that the overall intent of the proposals has received general support. However, when voted on the original proposal (DCP066) received limited support whereas the alternative proposal (DCP066A) received a large majority of support from DCUSA parties. The Authority has considered the issues raised by the change proposal, the Change Report and the Change Declaration⁷ issued on 2 December 2010. The Authority has concluded that:

1. DCP066A should be implemented as opposed to DCP066;
2. implementation of DCP066A will better facilitate the achievement of relevant objective (b) of the DCUSA; and
3. DCP066A is also consistent with the Authority's principal objective and statutory duties.⁸

Reasons for the Authority's decision

We have considered whether the provision of additional forecast information pertaining to future allowed revenue and distribution charges better facilitates the achievement of the relevant objectives of the DCUSA and is consistent with the Authority's principal objective and statutory duties. We have also considered whether a monthly or quarterly provision of this information, as proposed by DCP066 and DCP066A respectively, better facilitates the relevant objectives.

After reviewing the DCUSA applicable objectives, we agree with the working group and consultation respondents, that applicable objective (b) is pertinent to this decision.

DCUSA objective (b) – The facilitation of effective competition in the generation and supply of electricity and (so far as is consistent with that) the promotion of such competition in the sale, distribution and purchase of electricity

⁶ As set out in the Distribution Licence Standard Condition 22.2, see:

<http://epr.ofgem.gov.uk/index.php?pk=doc602057>

⁷ All documents can be accessed via the DCUSA website: <http://www.dcusa.co.uk/Extranet/CP.aspx?id=93>

⁸ The Authority's statutory duties are wider than matters that the Panel must take into consideration and are detailed mainly in the Electricity Act 1989 as amended as well as obligations arising under EU legislation.

Requirement for new information (Tables 1 and 2)

According to respondents to the Panel's consultation, the proposals will help Suppliers and IDNOs improve the accuracy of their forecasts, provide greater certainty of future charges and, in the case of suppliers, enable them to compete more effectively due to the enhanced data provision. Although most DNO respondents were supportive of the general aim of the change proposals, they raised concerns regarding the added value to users of providing High and Low estimates for a number of volatile items in Table 2 of Schedule 15. They believe such information is likely to be excessive for all but the largest suppliers, and may be misleading. One respondent stated that the proposal would not help promote competition in supply, but may serve to strengthen the dominance of large players, who are best placed to interpret and respond to frequent information.

We consider that the provision of forecast information relevant to the calculation of distribution charges would better facilitate competition between Suppliers. In particular, the additional transparency provided by this information should give an equal opportunity to forecast future UoS charges regardless of the stakeholders' company size. If the information is robust, it should also improve the accuracy of their own forecasts and assessments, which should lead to more informed business plans and pricing strategies. In addition, by making forecasts of future charges more accurate, Suppliers will face less uncertainty with respect to future changes in UoS charges and be exposed to less risk.

Regarding the provision of High and Low estimates for volatile items, we consider that DNOs should be able to provide better estimates of their costs than Suppliers or other stakeholders are able to. Such information can be useful in order to assess the reliability of revenue forecasts and their potential deviation from the forecasted value. While the value of these costs may not always be certain in advance, the DNOs' best attempts to forecast them can provide valuable signals to Suppliers and IDNOs of the likelihood and scale of changes in charges. We note that DNOs are separately working on assessing and mitigating volatility in use of system charges through another industry working group.⁹

Overall, we consider that additional information should reduce costs and uncertainty to Suppliers. This in turn should reduce barriers to entry into the supply market, enhance competition and benefit customers.

Reporting frequency (Table 1 only)

With regard to the proposed frequency and timing of reporting the information provided in Table 1 under Schedule 15, we favour an approach that strikes the right balance between timely provision of robust data and minimal administrative cost for the parties involved.

We note the preference of most Suppliers for a monthly disclosure of Table 1 which could be used for pricing contracts on more up-to-date information. They note that in the past, numbers have moved significantly between quarterly reporting representing an additional risk on Suppliers. They believe that by changing the frequency of the submissions to a monthly basis, they could get a timely indication of any material changes to charging and reduce the risk of mispricing contracts.

⁹ In particular, the Energy Networks Association organises a group called Workstream C. The Workstream is responsible for reviewing and developing long term products and arrangements for managing volatility in UoS charges.

DNOs and some members of the working group noted that the revenue information does not tend to change on a monthly basis; hence a quarterly disclosure should be both cost effective and provide Suppliers with the right amount of information necessary to understand the existing reports and minimise the level of uncertainty around future DUoS charges. We note that Suppliers have the opportunity to question the accuracy and consistency of this information in the quarterly DCP50 teleconferences. In regard to the timing of the information provision, DNOs believe that the timing of the publication set out in DCP066A would be more in line with their own internal re-pricing and price control reporting work.

We also note DNO respondents who considered that monthly reporting would require significant resources. They argued that monthly reporting will add costs for the DNOs and for the DCUSA: for example, DCUSA already estimated an additional cost of £6,000 per year solely related to the additional publications necessary above the existing quarterly uploads.

We are sympathetic to Suppliers' concerns in relation to the volatility of DNOs' revenues and UoS charges and agree that more frequent reporting may mitigate these concerns. However we consider that insufficient analysis has been presented to us to assure us that the additional costs associated with monthly reporting of Table 1 are proportionate, given the expected additional benefits. We consider that any further proposal to introduce more frequent reporting would need to be accompanied by more detailed analysis and justification.

Decision notice

After reviewing both the consultation and RFI responses, we consider that both DCP066 and DCP066A seek to improve the provision of relevant information on revenues and charges. They both better assist the objective of facilitating effective competition and would be an improvement to the DCUSA baseline. The improved reports will enable Suppliers and IDNOs to better understand DNOs' forecasts and changes to UoS charges.

We have decided to approve DCP066A because it aligns reporting with DNOs' internal re-pricing and price control reporting, and because there is insufficient analysis to allow us to approve the monthly reporting included in DCP066. Because it is important that DNOs give timely notice of changes in their revenue, we are supportive of Parties considering whether further development of reporting requirements (eg by introducing monthly reporting for some or all data in Tables 1 and 2) may be appropriate should DCP066A prove to be insufficient. Should a further proposal be developed we would expect more convincing analysis of the costs and benefits of further changes to the reporting requirements.

We also consider that DCP066A is consistent with Ofgem's principal objective to protect the interests of consumers, wherever appropriate by promoting effective competition.

In accordance with standard licence condition 22.2b of the Electricity Distribution Licence the Authority hereby directs that modification proposal DCP066A: 'Enhanced Provision of Cost Information' is made. The implementation date for DCP066A is 28 January 2011.

Rachel Fletcher
Director, Distribution

Signed on behalf of the Authority and authorised for that purpose