



DCUSA CONSULTATION

DCP 178 - Notification Period for Change to Use of System Charges

1 Purpose

- 1.1 The Distribution Connection and Use of System Agreement (DCUSA) is a multi-party contract between electricity Distributors and electricity Suppliers and large Generators. Parties to the DCUSA can raise Change Proposals (CPs) to amend the Agreement with the consent of other Parties and (where applicable) Ofgem.
- 1.2 This document is a Consultation issued to Distributors, Suppliers, Consumer Focus, Ofgem and other interested Parties seeking industry views on DCP178 'Notification period for change to use of system charges'. You are invited to consider the questions set out in section 8 below and submit comments using the form attached as Appendix A to dcusa@electralink.co.uk. Alternatively, responses can be submitted via the online form which is available here:

<https://www.surveymonkey.com/s/DCP178>

- 1.3 Responses to this consultation should be submitted no later than **29 October 2013**.

2 Background

- 2.1 Distribution Network Operators (DNOs) are currently required to finalise and publish Distribution Use of System (DUoS) tariffs 40 days before they take effect. DCP 178 'Notification Period for Change to Use of System Charges' has been raised by Northern Powergrid and seeks to increase this notice period from 40 days to 15 months. This change would provide Suppliers and consumers with greater certainty of future DUoS charges they will face.
- 2.2 Any over/under recovery of allowed revenue which arises because of the increased notice period would be recovered in future years.
- 2.3 The CP has been raised following on from industry discussions on how to mitigate the impact of DUoS tariff volatility. Ofgem, in their 2012 volatility paper¹, suggested bringing forward the notice period for the publication of

¹<https://www.ofgem.gov.uk/ofgem-publications/50572/cvdecision.pdf>

tariffs and this idea has also been discussed at various industry forums. Currently, DNOs under their licence are required to provide 3 months' notice of a change to their DUoS charges (this is generally in December and these are commonly known as Indicative Charges). This is followed by a 40-day notice period under DCUSA (mid-February commonly known as Final Charges). Initial thinking, was to align the two notice periods, which would effectively mean only one publication in December and would provide more notice to suppliers than the current 40 days. DCP 178 goes a step further in that it proposes to provide 15 months' notice, effectively setting final charges 1 year ahead, and indicative tariffs would no longer be required.

- 2.4 Full details of the Change Proposal (CP) are provided in the CP form (Appendix B) and additional information is available in the discussion paper "Options for notifying use of system charges fifteen months in advance of price changes coming" (Appendix C).

3 Working Group Assessment of DCP 178

- 3.1 The DCUSA Panel established a Working Group to assess DCP 178. The group consists of Distributor, Supplier, Consumer and Ofgem representatives. The topics discussed by the Working Group are detailed below.

Potential Benefits of the Change Proposal

- 3.2 The Working Group agreed that increasing the notice period for DUoS tariffs from 40 days to 15 months may have significant benefits for Suppliers and Consumers. Tariffs will be more predictable and transparent and there will be improved certainty over future short term DUoS charges. This could also lead to reductions in the charges some customers pay for DUoS in their contract.
- 3.3 To illustrate, currently if a Supplier offers a two year contract to a customer in January of any year for a two year contract from the following April they run the risk of the charges changing 7 times through that period, in line with the indicative and final publication of DUoS tariffs. (Note: The number of changes to DUoS tariffs will reduce from April 2015 with the removal of within year price changes but this will still leave three possible price changes within the period of the contract). These changes can be significant.

- 3.4 There are two types of contract that a customer can enter into with the Supplier. The first is an all-inclusive contract which will incorporate DUoS charges. The second is a pass through contract where the DUoS charge is passed straight through to the customer by the Supplier.
- 3.5 For an all-inclusive, non-pass through contract customer (where the DUoS charge is fixed into the overall rates that the customer pays) the Supplier bears all the impact of the change to charges (unless the Supplier has a claw back clause in their terms & conditions).
- For example, the Supplier may charge the customer an additional premium to cover their risk around these changes to DUoS charges.
 - Whereas, non-pass through customers are not impacted by any changes to DUoS charges as the Supplier bears the risk but the customer may be paying more in risk premia to be protected from these changes.
- 3.6 For a pass through contract customer (where the customer pays the actual DUoS charge) the customer bears the risk and uncertainty of DUoS charges changing over the period of the contract.
- 3.7 It was noted that improved notice of DUoS tariffs will potentially enable Suppliers to:
- Introduce new products, in particular non-pass through of DUoS contracts for EHV consumers. Currently, it is unlikely that Suppliers offer such contracts as the risk associated with them is too high.
 - Reduce the risk premium in existing DUoS non-pass through products, as there will be more certainty on the DUoS element of these charges.
 - Improved notice of DUoS tariffs will enhance the ability of Suppliers to forecast and budget for DUoS charges.
- 3.8 Consumers will benefit as:
- Non-pass through consumers will potentially face lower charges from Suppliers because Suppliers will not have to include such risk premiums

into the DUoS element of their products.

- It may potentially widen the product range available to non-pass through consumers as they may be more willing to take pass through contracts.
- Improved notice of DUoS tariffs will enhance the ability of consumers on pass through contracts to forecast and budget for DUoS charges.
- EHV consumers will potentially be offered a greater range of products to choose from, as non-pass through of DUoS contracts may become available.

Impact on Recovery of Allowed Revenue

3.9 The method used to calculate DUoS tariffs is defined within DCUSA Schedule 16, Schedule 17 and Schedule 18. The method is intended to enable DNOs to recover their “allowed revenue” for the charging year in a cost reflective manner. The “allowed revenue” for all DNOs is set by Ofgem for a pre-determined period known as the Distribution Price Control Period. Currently this covers 5 years from 2010-2015, going forward allowed revenue will be known for 8 years from 2015-2023.

3.10 Two concerns were expressed by the group around this area:

- All DNO members of the Working Group highlighted concerns around the potential increased risk of large over/under recovery of allowed revenue and the associated penalties; and
- One DNO member of the Working Group expressed concerns that this could also lead to an impact on the cost of capital for their business. This was not identified as an issue for rest of the DNOs.

3.11 A consumer representative on the Working Group suggested that the benefits of this modification to consumers were far greater than the dis-benefits to DNOs, as they will be able to factor this more accurately into their budget and forecasting processes.

3.12 Further details on the concerns raised by one DNO around the cost of capital are provided in Appendix D.

- 3.13 The increased risk of over/under recovery was a concern raised by all DNOs. By bringing forward the publication date of final tariffs there is an increased risk that DNOs will not recover their allowed revenue for each charging year. This is because they will be forecasting their income recovery over a longer period of time, thus making them more exposed to unforeseen environmental (weather) and economic changes. This could result in increases in over/under recovery of revenue which would then be recovered in future years.
- 3.14 However, DNOs are subject to licence conditions that penalise them for over/under recovery of revenue outside of the tolerances determined in their licence. Further details on these penalties can be found in paragraph 7 of Appendix C. They are also discussed under section 4 below.
- 3.15 The Working Group noted that the ability of DNOs to change their tariffs will be restricted to once a year from April 2015. In recognition that this will reduce DNOs' ability to recover their allowed revenue within the charging year, Ofgem has proposed that the penalty band thresholds within the distribution Licence be doubled.
- 3.16 The group discussed whether this proposed Licence change would be sufficient to alleviate DNO's concerns with regards to DCP 178. It was suggested that a further change to the penalty rate as well as the penalty bands may be required. The group noted that such a change might be considered reasonable given that under DCP 178 DNOs would not have the opportunity to change the tariffs other than once a year.
- 3.17 It was highlighted by a Working Group member that from a DNO viewpoint this change would increase the risk to DNOs of breaching the over/under recovery thresholds and any changes to this would need to be progressed through a Licence change. It was noted that a Licence change is outside the scope of the DCP 178 Working Group, but that Ofgem has already proposed that the penalty band thresholds within the distribution Licence be doubled to reflect that from 1 April 2015 DNOs will only be able to change tariffs once a year.
- 3.18 To aid in understanding the potential impact on DNOs' risk exposure, the Working Group undertook some analysis based on historic over/under recovery data. This analysis is documented in section 4 below.

What happens if there is an Error in Published Tariffs?

- 3.19 The Working Group considered what would happen under DCP 178 should there be an error in the tariffs published by DNOs. The group noted that in the past errors have occurred which have resulted in changes to published tariffs. These errors occurred soon after the CDCM was introduced. It was observed that now that the CDCM has been in place for a number of years, DNOs are in a steady state with regards to the calculation of DUoS tariffs and increasingly robust error checking methods are being tried, tested and developed. The risk of errors occurring in the published tariffs has therefore reduced over time.
- 3.20 Where an error does occur, a DNO can request a derogation from Ofgem seeking permission to publish a revised set of tariffs, although the Working Group noted that the impact would need to be significant for Ofgem to approve such a change. With DCP 178 in place tariffs would be calculated and published sooner, therefore, increasing the likelihood that errors would be identified earlier rather than later.
- 3.21 The group noted that DCP 104² was raised in 2011 seeking to put in place a framework for the correction of manifest errors in DUoS charging. This CP was rejected by Ofgem on the basis that it did not better facilitate the DCUSA Charging Objectives. The group agreed that a process for addressing manifest errors should not be incorporated into the DCP 178 legal text as this is outside of the scope of DCP 178.

Interaction with other DCUSA Change Proposals

- 3.22 The aim of this change is not to stop any changes to the charging methodology being progressed in a timely manner. The intent is to provide some stability and predictability in the tariffs for the benefit of both suppliers and end customers. Each DCUSA change is assessed on its own merits and the Working Group agrees the most appropriate implementation date.
- 3.23 Prior to charging methodology changes being submitted to DCUSA, many of the changes have been assessed by the Distribution Charging Methodology Forum (DCMF) issues sub-group in order to assess the priority of the proposed

² DCP 104 - Shared Impact of Manifest Errors in DUoS Charging.

changes and ensure that changes are both viable and capable of being approved. In order to keep disturbance in tariffs manageable and avoid mid-year tariff changes, it was agreed that implementation dates for methodology changes which have an impact on tariffs, should have an implementation date of 1 April in any given charging year.

3.24 This change was discussed at the DCMF issues sub-group prior to submission to DCUSA.

3.25 There are currently several changes in the development process and the majority of these are looking for an implementation dates of April 2015 at the earliest. So if this change were to be implemented then these changes should already have been either approved or rejected in time to be included in charges in December 2014.

3.26 DCP 178 would apply to all CDCM and EDCM DUoS tariffs, i.e. Extra-High Voltage (EHV), High Voltage (HV) and Low Voltage (LV) tariffs.

Implementation of Future Change Proposals

3.27 Should DCP 178 be implemented, then the timeline for the implementation of future DCUSA CPs that affect DUoS tariffs will need to be extended to accommodate the requirement to give 15 months' notice of new tariffs.

3.28 This will mean that where a CP is approved it will not be incorporated into the calculation of DUoS tariffs for at least 15 months after approval. However, there is already precedent set within the methodology to provide 15 months' notice for certain inputs so this change would complement that timeline.

4 DNO Risk Exposure

4.1 The Working Group notes that the distribution licence Charge Restriction Condition (CRC)¹⁴ details the bandwidths for over/under recovery and in simplistic terms penalty interest rates apply if the DNO is over or under recovered by 3% from their Allowed Revenue number for any given Regulatory Year (clause 14.2).

4.2 Having sought Ofgem's guidance, the group understand this clause will be

revised to 6% under RIIIO-ED1. This is to take account of the Ofgem decision to limit DNOs to one tariff change per year removing the ability to introduce a mid-year change.

- 4.3 The Working Group sought data from DNOs on their historic levels of over/under recovery of allowed revenue. This data is provided as Appendix F. The historical over/under recovery values demonstrate that there are not many instances outside the +/-6% band, where DNOs were over/under recovered by a significant value. Although, in this historical data DNOs had the ability to make mid-year price changes which would reduce the amount of over/under recovery in each year.
- 4.4 When looking at the data for all DNOs since the start of Distribution Price Control Review (DCPR) 5, no party has been subject to any penalty interest payments, with the 3% band width in place. However, we need to consider whether or not doubling the band width (from 3% to 6%) will be sufficient when the charges are published fifteen months in advance.
- 4.5 As an example, if the charges for 2016/17 are set in December 2014, the first year when the DNO will be able to reflect the final recovery position for 2016/17 will be at the point when the charges for 2019/20 are being calculated (see table below). Note that final tariffs for the next two years would need to be produced, but only one set thereafter.

Charge Setting Date	Period Charges Published for	Period when Final Recovery Period known
December 2014	2016/17	2013/14
December 2015	2017/18	2014/15
December 2016	2018/19	2015/16
December 2017	2019/20	2016/17

- 4.6 Ofgem has informed the Working Group that if the 6% threshold is seen to be insufficient then it would be for DNOs to seek a change, providing good justification as to why the thresholds should be further revised.

5 Assessment against the DCUSA Objectives

- 5.1 For a DCUSA Change Proposal to be approved it must be demonstrated that it better meets the DCUSA Objectives. There are five General DCUSA Objectives and five Charging Objectives. The full list of objectives is documented in the CP form provided as Appendix B.
- 5.2 The Working Group has assessed the CP against the DCUSA objectives and believes that the following DCUSA Objectives are better facilitated by DCP 178.

General Objective 2 - The facilitation of effective competition in the generation and supply of electricity and (so far as is consistent therewith) the promotion of such competition in the sale, distribution and purchase of electricity

- 5.3 General Objective 2 is better facilitated by ensuring increased stability and transparency within the Charging Methodology. This in turn, should increase market confidence in the tariff setting regime and encourage competition by reducing price shocks for Suppliers (both new entrants and current participants) and consumers.

Charging Objective 2 - that compliance by each DNO Party with the Charging Methodologies facilitates competition in the generation and supply of electricity and will not restrict, distort, or prevent competition in the transmission or distribution of electricity or in participation in the operation of an Interconnector (as defined in the Distribution Licences)

- 5.4 Charging Objective 2 is better facilitated as the CP ensures increased stability and transparency within the Charging Methodology. This in turn, should increase market confidence in the tariff setting regime and encourage competition by reducing price shocks for Suppliers (both new entrants and current participants) and consumers.

6 DCP 178 Implementation Date

- 6.1 Under RIIO-ED1³ Ofgem will notify DNOs of their allowed revenue for the years 2015 to 2023 by February 2014 at the earliest. To enable DNOs to give 15 months' notice of the DUoS tariffs that are to take effect from 1 April 2015, tariffs would have to be published in December 2013. This is not possible under the RIIO-ED1 timescales as DNOs will not know their allowed revenue, which is needed to calculate tariffs, by December 2013.
- 6.2 Given that DNO revenues under RIIO-ED1 will not be confirmed by Ofgem until February 2014 at the earliest, the implementation date proposed for DCP 178 is December 2014, such that the first set of tariffs for which there will be a 15 month notice period are those that take effect from 1 April 2016.
- 6.3 The expectation of the Working Group is that the final tariffs for April 2015 will be published 3 months in advance rather than 40 days (i.e. final tariffs will be published in December 2014 rather than February 2015). This would mean that both the April 2015 and April 2016 final tariffs would be published in December 2014. As part of this consultation you are invited to provide your views on this approach.

7 DCP 178 Legal Drafting

- 7.1 The proposed legal text for DCP 178 is provided as Appendix E.
- 7.2 The legal text amends the notice period for the publication of tariffs from 40 days to 15 months. This is achieved by amending the notice period specified in DCUSA Clause 19.1 and adding a new paragraph to Schedule 16, Schedule 17 and Schedule 18 stating that all inputs to the charging methodologies must be confirmed and used in the DUoS charges as published under Clause 19.1.
- 7.3 An amendment is also made to Schedule 16 paragraph 43 and paragraph 49 to clarify that when determining load characteristics for demand users and peaking probabilities, DNOs should seek to use data for the most recent 3 year period at the time of setting charges for the relevant charging year.

³ RIIO-ED1 is the Electricity Distribution price control review period starting 1 April 2015. Information on RIIO-ED1 can be found on Ofgem's website here:

<http://www.ofgem.gov.uk/Networks/ElecDist/PriceCtrls/Pages/PriceCtrls.aspx>

7.4 Legal text that was added by approved DCUSA CPs DCP 136⁴ and DCP 150⁵ is also removed in the DCP 178 legal text. The legal text associated with these two CPs is as follows:

- DCP 136: DCUSA Schedule 16 - last two sentences of paragraphs 19 and 33.
- DCP 150: DCUSA Schedule 16 paragraphs 25A, 28A, 35A and 51A

7.5 DCP 136 and DCP 150 introduced 15 month notice periods for certain inputs into the calculation of DUoS tariffs. If DCP 178 is approved these notice periods for certain CDCM inputs will no longer be required.

8 DCP 178 – Consultation Questions

8.1 The Working Group has split the questions for this consultation into two parts as follows:

- **Part 1 – Questions for consumers:** these questions are intended for electricity consumers only.
- **Part 2 – Questions for all interested parties:** these questions are intended for all interested parties. Consumers can opt to provide answers to either Part 1 only or both Part 1 and Part 2.

8.2 The consultation questions are as follows:

No.	Question
Part 1 – Questions for Consumers	
1	Do you support this change?
2	What benefits do you believe it will bring to your organisation?
3	Do you agree with the proposed implementation date of December 2014? Please provide your rationale.
4	Do you believe that the April 2015 tariffs published in December 2014 should be final tariffs, rather than indicative tariffs?
5	This Change Proposal proposes a 15 month notification period. Do you agree with this timescale or do you believe that an alternative should be considered? Please provide your rationale.
6	Do you have any concerns about the change?
7	Please state any other comments or views on the Change Proposal.

⁴DCP 136 - Notice period for asset cost changes in the CDCM

⁵DCP 150 - Implementation of Notice in DCUSA for Changes to certain CDCM Inputs

Part 2 – Questions for all interested parties	
8	Do you understand the intent of the CP?
9	Are you supportive of the principles established by this proposal?
10	Are there any unintended consequences of this proposal?
11	One DNO has expressed concern about the cost of capital and some DNOs have expressed concerns about under/over recovery thresholds (which are detailed in Ofgem's volatility paper - 2012). What are your views on these concerns?
12	Do you consider that the proposal better facilitates the DCUSA objectives? Please give your rationale.
13	Do you agree with the proposed implementation date of December 2014? Please provide your rationale.
14	Do you believe that the April 2015 tariffs published in December 2014 should be final tariffs, rather than indicative tariffs?
15	This Change Proposal proposes a 15 month notification period. Do you agree with this timescale or do you believe that an alternative should be considered? Please provide your rationale.
16	A significant number of the CDCM inputs already require 15 months' notice to update them ⁶ ; DCP 178 would mean that this period would apply to all inputs to both the CDCM and EDCM model. The majority of the Working Group believe that the benefits of DCP 178 outweigh any potential delay in implementing other charging methodology changes, do you agree?
17	Do you have any comments on the proposed legal text?
18	Do you have any further comments?

8.3 Responses to this consultation should be submitted no later than **29 October 2013**. You can provide your response by sending the form provided in Appendix A to dcusa@electralink.co.uk. Alternatively, you can submit your responses using the online form which is available here:

<https://www.surveymonkey.com/s/DCP178>

8.4 Responses, or any part thereof, can be provided in confidence. Parties are asked to clearly indicate any parts of a response that are to be treated confidentially.

9 Next Steps

⁶ In accordance with DCUSA Change Proposals DCP 150, DCP 136 and DCP 134.

- 9.1 Responses to the Consultation will be reviewed by the DCP 178 Working Group. The group will use the responses received to aid it in its development of the CP.
- 9.2 If you have any questions about this paper or the DCUSA Change Process please contact the DCUSA by email to dcusa@electralink.co.uk or telephone 020 7432 2842.

Appendices

- Appendix A – Response Form
- Appendix B – DCP 178 CP Form
- Appendix C – Discussion paper - Options for notifying use of system charges fifteen months in advance of price changes coming
- Appendix D – DNO Under/Over Recovery Impact on Cost of Capital
- Appendix E - Proposed Legal Text
- Appendix F – DNO Under/Over Recovery Data