

Proposed variation:	<b>Distribution Connection and Use of System Agreement (DCUSA) DCP232 – GP and GL Solution</b>		
Decision:	The Authority <sup>1</sup> directs this modification <sup>2</sup> be made <sup>3</sup>		
Target audience:	DCUSA Panel, Parties to the DCUSA and other interested parties		
Date of publication:	04 November 2015	Implementation date:	01 April 2016

## Background

This proposal concerns two terms that were removed from Special Condition 11 (also known as 'Charge Restriction Condition' (CRC) 11) of the electricity distribution licence from 1 April 2015. These terms related to revenues from distributed generation incentives during the two preceding price control periods (DPCR4<sup>4</sup> and DPCR5<sup>5</sup>).

The terms are reflected in the calculation of generator revenue in the Extra high voltage Distribution Charging Methodology (EDCM). The terms in the EDCM are:

- GL:** This relates to DPCR4 generation revenue. This is revenue related to generation connected to the distribution system between 2005 and 2010, reflecting the generation incentive scheme that was in effect at this time.
- GPa:** This value relates to DPCR5 generation pass-through revenue. This is based on the amount of use of system capital expenditure for generation that was subject to the pass-through arrangement under the DPCR5 price control.

Our most recent electricity distribution price control (RIIO-ED1) removed these terms from the licence. The legacy values have been carried forward into the current RIIO period but spread over the price control period. Therefore from 1 April 2015 there is no value in the licence relevant to these EDCM terms. This means the EDCM reference is inconsistent with the licence.

This inconsistency between the EDCM and the current licences was first identified in November 2014. In order to meet the deadline for the publication of 2015/16 charges, the distribution network operators (DNOs) calculated charges on the basis that these values would effectively be zero for charging year 2015/16 because of the changes to the licence.

The proposer of this DCUSA change proposal considers that this interpretation should continue but be formalised for future charging years.

## The modification proposal

DCP232 was raised by Western Power Distribution Limited on 11 February 2015. It proposes:

- a) To set the values of GL to zero from (and including) charging year 2015/16
- b) To set GPa to zero from (and including) charging year 2015-16.<sup>6</sup>

The modification was developed and consulted on by the DCUSA working group. In the initial consultation the working group considered two options:

<sup>1</sup> References to the "Authority", "Ofgem", "we" and "our" are used interchangeably in this document. The Authority refers to GEMA, the Gas and Electricity Markets Authority. The Office of Gas and Electricity Markets (Ofgem) supports GEMA in its day to day work. This decision is made by or on behalf of GEMA.

<sup>2</sup> 'Change' and 'modification' are used interchangeably in this document.

<sup>3</sup> This document is notice of the reasons for this decision as required by section 49A of the Electricity Act 1989.

<sup>4</sup> Distribution Price Control Review 4 ran from 1 April 2005 – 31 March 2010.

<sup>5</sup> Distribution Price Control Review 5 ran from 1 April 2010 – 31 March 2015.

<sup>6</sup> The value in the model for GPa is the average of GPa (aGPa) for the charging year and the two preceding charging years. Consequently, for charging year 2015/16 this value shall be the average of the GPa values for charging year 2013/14, 2014/15 and 2015/16, the latter being a zero value. For charging year 2016/17 aGPa will be the average of the GPa for 2014/15 plus two zero values for 2015/16 and 2016/17.

- a) To make the values GL in the EDCM to refer to the values as scheduled in the DPCR5 licence, ie a continuation of the DCPR5 approach.
- b) To set the GL values to zero.

Under both options the GPa value would be set to zero for charging years 2015/16 onwards.

Five out of six respondents supported option b), one respondent supported option a). The supporter of a) considers that it is more closely aligned with the licence whereas those supporting option b) assume that there is no incentive revenue in the charging year. Another respondent who had a preference for option b) considered that, in their network areas, the majority of generators have connected since 2010 with a large proportion connecting in the last couple of years. This meant that if the GL was not equal to zero then the majority of generators would be paying through the EDCM for an incentive that was actually due to a minority of them.

The working group conducted an impact assessment comparing the two options. For five DNO areas there were no differences between the two options. For the remaining DNOs, option b) results in lower capacity charges (ranging from 16% to 92%) for generators than would be the case for option a). Due to commercial confidentiality issues, the total value of these differences are not included in the impact assessment. The net impact of these reductions would be spread over all consumers.

The working group considered the argument presented by the supporter of option a). Although the DNOs could determine the values for the GL term under the DPCR5 legacy mechanisms<sup>7</sup>, the working group agreed that they would not be material and that option b) was the preferred approach. The working group decided to proceed with option b).

All members of the working group and the consultation responses stated that they believe that this proposal better facilitates DCUSA Charging Objective 3.2.1<sup>8</sup> in that this proposal is aligned with the current RIIO-ED1 licences.

## **Process to date**

The initial Change Declaration dated 25 August 2015 recommended that we reject DCP232 because only one supplier voted and they voted against the proposal. The DCUSA voting procedures require that in order to be accepted, in the majority of the party categories that are eligible to vote, the sum of the weighted votes of the groups in each party category which voted to accept the implementation date is greater than 50%.

### Send back decision

On 30 September 2015, we sent the proposal back to the DCUSA Panel because the legal text incorrectly referred to 2014/15 instead of 2015/16 in reference to setting the GL term to zero. We directed the Panel to revise the legal text and resubmit to us for decision as soon as possible.

The revised proposal was issued to the industry for voting on 15 October 2015. The only change to the proposal was to amend the legal text to refer to 2015/16.

We received the new change declaration for our decision on 23 October 2015. Unlike the change declaration from 25 August 2015, the recommendation this time was to accept

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<sup>7</sup> Mechanisms are set out in the ED1 Price Control financial Handbook:

[https://www.ofgem.gov.uk/sites/default/files/docs/2015/02/ed1\\_handbook\\_slowtrack\\_feb2015\\_0\\_1.pdf](https://www.ofgem.gov.uk/sites/default/files/docs/2015/02/ed1_handbook_slowtrack_feb2015_0_1.pdf)

<sup>8</sup> DCUSA Charging Objective 3.2.1 – that compliance by each DNO Party with the Charging Methodologies facilitates the discharge by the DNO Party of the obligations imposed on it under the Act and by its Distribution Licence.

the proposal. This is because the supplier party who voted against the proposal previously did not vote this time. We have considered their previous comments in the section on the reasons for our decision.

### DCUSA Parties' recommendation

The Change Declaration for DCP232 indicates that all parties were eligible to vote on DCP232. In each party category where votes were cast (no votes were cast in the DG, IDNO/OTSO<sup>9</sup>, supplier or gas supplier<sup>10</sup> party categories) there was unanimous support for the proposal and its proposed implementation date. In accordance with the weighted vote procedure, the recommendation to the Authority is that DCP232 is accepted. The outcome of the weighted vote is set out in the table below:

DCP232	WEIGHTED VOTING (%)							
	DNO		IDNO/OTSO		SUPPLIER		DG	
	Accept	Reject	Accept	Reject	Accept	Reject	Accept	Reject
CHANGE SOLUTION	100%	0%	n/a	n/a	n/a	n/a	n/a	n/a
IMPLEMENTATION DATE	100%	0%	n/a	n/a	n/a	n/a	n/a	n/a

### Our decision

We have considered the issues raised by the proposal, the Change Report and Change Declaration dated 23 October 2015. We have considered and taken into account the vote of the DCUSA Parties on the proposal which is attached to the Change Declaration. We have concluded that:

- implementation of the modification proposal will better facilitate the achievement of the DCUSA Charging Objectives;<sup>11</sup> and
- directing that the modification be made is consistent with our principal objective and statutory duties.<sup>12</sup>

### Reasons for our decision

We consider this modification proposal will better facilitate DCUSA Charging Objective 3.2.1 and has a neutral impact on the other relevant objectives.

#### ***DCUSA Charging Objective 3.2.1 – that compliance by each DNO Party with the Charging Methodologies facilitates the discharge by the DNO Party of the obligations imposed on it under the Act and by its Distribution Licence***

We consider DCP232 better facilitates Charging Objective 3.2.1. We agree that the change in treatment of DG incentive revenues in RIIO-ED1 should be reflected in DCUSA. We also agree with the working group's consensus that option b) is the preferred solution as it is consistent with the new licence conditions.

We note in the initial change declaration of 25 August 2015 that one supplier party voted against DCP232. They stated that they do not consider it better facilitates this charging objective on the grounds that they consider the DNOs have not properly taken account of changes triggered by the implementation of the RIIO-ED1 licence with respect to the EDCM generation revenue pot.

<sup>9</sup> Independent Distribution Network Operator/Offshore Transmission System Operator

<sup>10</sup> There are currently no gas supplier parties.

<sup>11</sup> The DCUSA Charging Objectives (Relevant Objectives) are set out in Standard Licence Condition 22A Part B of the Electricity Distribution Licence and are also set out in Clause 3.2 of the DCUSA.

<sup>12</sup> The Authority's statutory duties are wider than matters that the Parties must take into consideration and are detailed mainly in the Electricity Act 1989 as amended.

We note that RIIO-ED1 changed the way DG incentive revenues from the two previous price controls were identified in the licence. We do not agree with the views of this supplier and consider that this proposal enables the licence change to be reflected in distribution use of system charges within the EDCM.

***DCUSA Charging Objective 3.2.3 – that compliance by each DNO Party with the Charging Methodologies results in charges which, so far as is reasonably practicable after taking account of implementation costs, reflect the costs incurred, or reasonably expected to be incurred, by the DNO Party in its Distribution Business***

The same supplier party considered that this objective was not better facilitated. This is because the proposed EDCM generation revenue pot will eventually no longer include any share of the allowances included in DNOs' base revenues associated with use of system capital expenditure for all EDCM generation or incentive and operation and maintenance allowances for generation connected between 2005-2010. This share of DNO revenue allowance will instead be picked up by demand customers. They considered that this represents a reduction in cost reflectivity.

We decided under RIIO ED1<sup>13</sup> not to specify DG incentive provisions included in DCPR5. While those values have been used in the past for allocating costs between generators and others, they are no longer available. This proposal is consistent with the decision made in RIIO ED1 where the ability to identify these specific charges and allocate them accordingly has been removed.

We consider that the proposal is neutral against this charging objective.

***DCUSA Charging Objective 3.2.4 – that, so far as is consistent with Clauses 3.2.1 to 3.2.3, the Charging Methodologies, so far as is reasonably practicable, properly take account of developments in each DNO Party's Distribution Business***

This supplier party also considered that this objective was not better facilitated on the grounds that they considered DNOs have not properly taken account of changes to their RIIO-ED1 licence with respect to the EDCM generation revenue pot. This party believed DNOs should be required to submit a revised change to properly take account of the changes in the RIIO-ED1 licence whilst maintaining an appropriate EDCM generation revenue target.

The licence following the RIIO-ED1 price control has removed these terms. Therefore this modification is taking account of this development. Should a party feel that a further modification is required to better allocate DG charges this can be put forward as a separate modification through the DCUSA open governance.

We consider that the proposal is neutral against this charging objective.

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<sup>13</sup> <https://www.ofgem.gov.uk/ofgem-publications/47068/riioed1decoutputsincentives.pdf>

## **Decision notice**

In accordance with standard licence condition 22.14 of the Electricity Distribution Licence, the Authority hereby directs that modification proposal DCP232: GP and GL Solution be made.

**Ian Rowson – Associate Partner: Regulatory Finance and Compliance**

Signed on behalf of the Authority and authorised for that purpose