

Assessment of Application of IDNO Charges to Licence Exempt Distributors

1 BACKGROUND

- 1.1 DCP 251 and DCP 252 propose that the Licensed Distribution Network Operator (LDNO) tariffs should apply to Qualifying Network Operators (QNOs), a newly proposed term for the Distribution Connection and Use of System Agreement (DCUSA). DNO Parties and IDNO Parties are required, by their licences, to be party to, comply with, and maintain this agreement. The following definitions are contained in the relevant schedules of the DCUSA and to aid the reader are also included in the glossary in Appendix 3.
- **DNO - Distribution Network Operator** means a Party that holds a Distribution Licence in which Section B of the standard distribution licence conditions has effect, whether or not that Party is also engaged in the supply or generation of electricity. (DCUSA Schedule 1A)
 - **IDNO - Independent Distribution Network Operator** means a Party that holds a Distribution Licence in which Section B of the standard distribution licence conditions does not have effect, whether or not that Party is also engaged in the supply or generation of electricity (DCUSA Schedule 1A)
 - **LDNO - Licenced Distribution Network Operator** a licensed distribution network operator, meaning an IDNO Party or DNO Party operating an electricity distribution system outside of its Distribution Services Area. (DCUSA Schedule 16 - CDCM)
- 1.2 The term QNO is intended to recognise that LDNO tariffs could apply to both IDNOs and DNOs who provide networks outside of their Distribution Services Area. However, the legal drafting suggests that licence exempt distributors could also fall under the definition of a QNO.
- 1.3 Throughout this document the latter are referred to as Distribution Exemption Holders (DEHs). To consider whether distribution systems operated under licence exemption should fall within the scope of a QNO, and therefore qualify for LDNO tariffs, it is important to consider:
- the services associated with use of system that a DEH may require in receiving use of system from the upstream licensed DNO to whose system it connects, compared to the services required by another licensed DNO connecting to the upstream licensed distribution system; and
 - to what extent the above is relevant to the applicability of the LDNO tariffs to the DEHs.
- 1.4 The Working Group noted that under Standard Licence Condition 18, DNOs have a duty to be able to provide metering point registration services in respect of any distribution system within its distribution services area. Since IDNOs do not have a distribution services area, they have a choice as to whether they offer such a service to licence exempt network operators connecting to their network. Therefore, licence exempt operators connecting to an IDNO network, or an out of area DNO network, may have to rely on the host DNO to provide such services.

- 1.5 The Working Group members agreed that use of system charges relate to the provision of use of system and the ancillary services associated with conveying electricity to and from the DNO boundary.
- 1.6 Provision of services on networks operated by licence exempt parties is outside of the scope of DCUSA as such operators are not party to the Agreement.

2 SCOPE OF DCP 251 AND DCP252

- 2.1 The scope of DCP 251 and DCP 252 is to consider:
 - introducing the term of Qualifying Network Operator (QNO) to define the different types of network operators that may be eligible for LDNO tariffs; and
 - the circumstances, if any, where DEHs should be entitled to be charged for use of system on the same basis as another licensed distributor; i.e. considered to be a QNO.
- 2.2 It is an important point to note that NHH traded sites on IDNO networks (or to DNO networks which are connected to another DNO network) are charged use of system on a portfolio basis and not on a site specific basis. DCP251 and DCP 252 do not seek to introduce a new IDNO methodology or to change charging arrangements in place for providing Use of System to other distribution networks. Rather, it seeks to clarify the types of networks that should qualify for the existing LDNO tariffs. It is also important to consider whether a licence exempt operator should be able to choose between the existing tariffs and the LDNO tariffs.
- 2.3 Out of scope of this DCP are:
 - changes to the charging methodologies (CDCM and EDCM);
 - changes to the charging mechanisms in place for providing Use of System to other distribution networks; and
 - facilitation of competition in supply (in whole or in part) on licence exempt networks.

3 THE IDNO METHODOLOGY

- 3.1 The common IDNO tariffs were established in 2010, following the introduction of the Common Distribution Charging Methodology (CDCM). Prior to this each DNO had their own methodology for charging IDNOs. These methodologies had been established and submitted to Ofgem on an interim basis on the understanding that the introduction of the CDCM would ensure commonality across all DNOs. See timeline in Appendix 2.
- 3.2 LDNO tariffs are currently only available to licenced distributors in respect of networks where they connect to a 'host' electricity distribution system. The tariffs are applied by the host licensee on a similar basis to how suppliers are charged i.e.:
 - On a portfolio basis for Non-Half Hourly (NHH) customers connected to LDNO owned distribution systems; and
 - On a site specific basis for Half-Hourly (HH) customers connected to LDNO owned distribution systems.
- 3.3 The DNO methodology for charges to IDNOs is on the following basis:
 - The IDNO provides the "last mile" of network and the associated services and obligations in operating such a network. In doing so it substitutes an activity that an incumbent DNO would otherwise have to do if it owned and operated that network. The term "last mile" is used to describe the network between a licensee's existing distribution system and the consumers' premises.

- In providing the last mile the IDNO is required to undertake and fund the activities in respect of that network that the upstream DNO would otherwise be required to undertake.
 - In undertaking those activities, the IDNO is allocated the same input costs/ charges that the upstream (incumbent) DNO would make to its own “notional business” if it owned and operated the last mile network; i.e. the “last mile” operator would be entitled to the same margin (if its charges to the consumer were the same as those of the incumbent). In this context margin means the difference between the prices charged by the incumbent DNO to the last mile operator and the charge applicable in respect of the end customer / consumer.
- 3.4 It is on the above basis that the Price Control Disaggregation Model (PCDM) has been developed. The PCDM attempts to allocate the total costs of providing, operating and maintaining a network to the different network tiers of the distribution system. It does this using Modern Equivalent Asset Value (MEAV) cost driver to determine a % allocation of costs to each network tier. The PCDM then calculates a discount factor based on what the last mile network operator (the IDNO) provides as a substitute. The discount factor reflects the deemed total avoided costs of the DNO because the IDNO is substituting the services that the DNO would need to provide if it owned and operated that network.
- 3.5 The PCDM is based on the incumbent DNO’s average costs for each network tier. This is consistent with the way that the DNO allocates its costs to the CDCM customers and sets its own tariffs (i.e. tariffs are set for different customer classes as an average across the DNO’s distribution services area).
- 3.6 The use of average costs has been an important and essential part of the consideration in developing IDNO charges. IDNO tariffs do not guarantee cheaper charges to all sites (when compared to the all the way tariffs) in all circumstances. Some sites, which if considered as a single traded entity, would be subject to a half hourly tariff. Where they have a high load factor they may have lower all the way charges than those prescribed by the PCDM.

4 COMPARING USE OF SYSTEM SERVICES FOR DIFFERENT NETWORK OPERATORS

- 4.1 In looking at whether tariffs for IDNOs should apply to licence exempt operators it is necessary to examine:
- whether the Use of System (UoS) services provided by the DNO to a DEH differ from those provided to IDNOs; and
 - to what extent the DEH, in operating their networks, requires additional Use of System services from the incumbent DNO compared to those required by the IDNO.
- 4.2 DEHs have an obligation to facilitate competition in supply where required to do so. How they procure or provide such services is outside the scope of this DCP.
- 4.3 In setting LDNO tariffs, step 4 of the CDCM, the PCDM, sets out the approach used to calculate the UoS charges applicable to IDNOs. DCP 251 and DCP 252 only consider whether the tariffs for IDNOs determined by this methodology should apply to DEHs. It is important to recognise that IDNOs are required to provide a number of services to facilitate competition in supply.
- 4.4 The provisional view of the Working Group is that under current industry arrangements it is unlikely that a DEH will be in a position to fully substitute the activities undertaken or fulfil the services that the DNO provides to the same extent as an IDNO in facilitating competition in supply (e.g. services relating to settlement, registration, supplier billing). Further licensees are required to fund Ofgem, the DCC and other industry parties, whereas DEHs are not.

4.5 Appendix 1 details some of the scenarios discussed by the Working Group:

- Table 1 - illustrates some of the activities and obligations that are required of a licensee in providing the last mile of network. It is therefore important to understand what these avoided services and obligations generate costs for parties that are determined within the CDCM.
- Table 2 - considers to what extent a LED would need to provide, procure and fulfil these obligations.
- Table 3 - covers scenarios where industry framework competition in supply arrangements are put in place for all or only a proportion of the customers connected to a licence exempt distribution system

5 SOME COMMENTS ON SERVICES

Creation of Meter Point Administration Numbers (MPANs)

- 5.1 The creation and management of MPANs is covered across various codes such as the MRA, BSC and DCUSA and through relevant settlement and registration systems. It is difficult to contemplate competition in supply on licence exempt networks without the upstream licensed DNO undertaking these services for and on behalf the DEH.
- 5.2 For a DEH there is likely to be an MPAN at the LDNO network/ licence exempt network boundary, a supplier appointed to the MPAN and for DUoS to be billed as for any other metering point. Where there is competition in supply on the licence exempt network there is still likely to be an MPAN at the boundary with additional MPANs being established for some customers being connected to the DEH. However, not all customers on the exempt network may have an MPAN. Therefore, difference metering arrangements will need to be in place. The charging for the facilitation of such arrangements is outside the scope of DCUSA and the charging methodologies.

Creation of Billing Data

Site Specific HH

- 5.3 For Half-Hourly (HH) traded sites, HH data will be provided by the Supplier to the DNO (this is because the DEH operator is unlikely to be capable of receiving data via the Data Transmission Network).

Portfolio Billing

- 5.4 For sites to be traded under Non-Half-Hourly (NHH) settlement arrangements portfolio billing will apply and consumption data would need to be maintained and collated in line with the portfolio tariffs. It is uncertain how a DEH would do this. This would likely require the establishment of unique Line Loss Factor Classes (LLFCs).

DUoS Liability

- 5.5 Arrangements for IDNOs are that the IDNO manages the relationship with the supplier. The IDNO is responsible for billing and collecting DUoS in respect of its own distribution system and in respect of the upstream licensed DNO; i.e. the IDNO bears the potential cash flow burden and business risk for supplier late payment/ failure:
- On what basis should a DEH be entitled to different charging arrangements from the IDNO?
 - If a DNO wishes to manage the DUoS billing and collection for a DEH then it would be required to do so on a basis that is not unduly discriminatory.

- The DNO will bill and collect DUoS from the appointed supplier in respect of conveying electricity to and from the DNO metering point/ exit point. However, where a DNO provides an MPAN for a customer connected to the DEH, Settlement will “deem” that the DNO is providing UoS across its own and the DEH system.

5.6 DCUSA covers the contractual arrangements in respect of a licensed distributor providing use of system to a supplier (or to another licensed distributor) in respect of its own distribution system. DEHs are not party to DCUSA, and as such there are no contractual provisions in DCUSA between a DEH and a supplier (or with a licensed distributor). Therefore, where a licensed distributor provides services to a DEH, such services are ultra vires the provisions of DCUSA. As a consequence:

- Should the provision of, and the charges for services provided by a DNO to a DEH be subject to separate arrangements outside the scope of the CDCM and DCUSA?
- Is the contractual relationship about how and on what basis a DEH bills a supplier ultra vires DCUSA provisions?

6 CONCLUSIONS

6.1 This paper is intended to provide some information and some discussion points for the DCP 251 and DCP 252 Working Group. The initial conclusions or initial position of this paper is by no means firm and further work is required to validate or reject the conclusions. The initial thoughts of this paper are as follows:

- A. The intent of DCP 251 and DCP 252 are about allowing QNOs to be eligible for LDNO tariffs. Therefore, the task of the workgroup is to determine the rules to be considered as a QNO.
- B. If a DEH demonstrates that it substitutes the DNO activity on a last mile network in the same way that an IDNO does then it should be considered as meeting the requirements to be considered as a QNO.
- C. If the DNO is providing services in respect of the customers connected to the DEH (for example, to facilitate competition in supply) then the DEH could:
 - a. be considered as a QNO and eligible for LDNO tariffs, but any services provided by the DNO in respect of such licence exempt network should be subject to separate contractual provisions (and charges);
 - b. be rejected as a QNO, and therefore not eligible for LDNO tariffs. Where such rejection is made the grounds for rejection need to be clear.

APPENDIX 1 - Comparing Use of System Services for Different Network Operators

THESE TABLES ARE ILLUSTRATIVE. IT DOES NOT DOCUMENT ALL THE SERVICES THAT ARE PROVIDED/ SUBSTITUTED BY A LAST MILE OPERATOR

1. The Working Group, in its efforts to highlight the differences or similarities between licensed network operators and licence exempt network operators has included the following tables in this report, representing different network scenarios.
2. The tables try to highlight the functions and activities that might be undertaken by a distribution network operator. Charges for these activities are only identified when they are over and above ordinary connection and use of system charges
3. Table 1 illustrates the services that a licensed DNO is mandated to provide in respect of end customers connected to its distribution system.
4. Table 2 illustrates the services that a DEH is required to provide in respect of customers connected to its licence exempt distribution system and where there is currently no competition in supply to customers on that system; i.e. the exit from the Total System is at the boundary between the licensed network and the private network:
 - Total System has the meaning ascribed to it in the Balancing and Settlement Code and means that an MPAN is allocated at the boundary from the licensed distribution system.
 - The relationship for the supply of electricity is between the customer registered to the MPAN (likely to be the DEH) and the supplier. End customers connected to the licence exempt network will have no contractual relationship with the licensed distributor or with the supplier (in respect of the traded MPAN)
 - The DEH is still bound by the 2011 regulations to allow third party access
5. Table 3 covers scenarios where industry framework competition in supply arrangements are put in place for all or only a proportion of the customers connected to a licence exempt distribution system:
 - End customers are allocated an MPAN
 - Where it is only some customers who are allocated an MPAN it is presumed that difference metering arrangements will be agreed between relevant suppliers. (Difference Metering arrangements are out of scope of this DCP)
 - The Working Group believe that it is only an LDNO that can provide an MPAN, and that in providing an MPAN the LDNO provides the services associated with it (e.g. registration services; production of LAFs etc.)
 - or where each exit point is registered in industry systems such that it can receive competition in supply. This is about a supply from a DEH unlicensed distribution system, for a large half hourly metered customer (measurement class C or E) that has a difference-metering BSC MPAN created by the regional DNO.
6. In addition to the three scenarios illustrated in the tables below, there is a potential fourth where a DEH network already exists but the DEH operator is not active. An example of this could be a housing tower block operated by the local authority, where:
 - no separate charging arrangements are in place to charge for the rising and lateral mains or any infrastructure within the building;

- it is likely that the DNO assumes responsibility for the customer's properties including wider services including emergency response and priority service arrangements; and
- the DNO charges the Supplier use of system charges for all of the properties connected to this 'unlicensed network', as if they were its own.

Table 1 - Services that a licensed distributor is mandated to provide in respect of end customers connected to its distribution system

Service	Is it required?	Who provides it?	Cost of service recovered as part of DNO/IDNO DUoS
Creation and maintenance of MPAN	Yes	LDNO	Yes
Coordination of change of supplier process (operating the registration system (MPRS))	Yes	LDNO	Yes
Energisation process ¹ (MPRS)	Yes	LDNO	Yes
BSC market domain data	Yes	LDNO	Yes
BSC loss adjustment factors	Yes	LDNO	Yes
Maintenance of agent appointments (MPRS)	Yes	LDNO	Yes
DCUSA as use of system agreement	Yes	LDNO	Yes
Receipt of settlement data for DUoS billing	Yes	LDNO	Yes
DUoS billing and collection to Suppliers	Yes	LDNO	Yes
Emergency call handling	Yes	LDNO	Yes
Emergency response	Yes	LDNO	Yes
Priority services and vulnerable customers where applicable	Yes	LDNO	Yes
UMSO where applicable	Yes	LDNO	Yes
DCC services charges	Yes	LDNO	Yes
Ofgem funding	Yes	LDNO	Yes

Notes

1. Energisation is the logical energisation as held in the MPRS system rather than a physical energisation on-site.

Table 2 - Services that a distribution exemption holder (DEH) is required to provide in respect of customers connected to its licence exempt distribution system and where there is currently no competition in supply to customers on that system

Service	Is it required?	Who provides it?	Cost of service recovered as part of DNO/IDNO	Charge Recovered by the PNO
Creation and maintenance of MPAN	No		No	No
Coordination of change of supplier process (operating the registration system (MPRS)) ¹	No	PNO	No	No
Energisation process (MPRS) ²	No	PNO	No	No
BSC market domain data	No		No	No
BSC loss adjustment factors	No		No	No
Maintenance of agent appointments (MPRS)	No		No	No
DCUSA as use of system agreement	No		No	No
Receipt of settlement data for DUoS billing	No		No	No
DUoS billing and collection to Suppliers	No	PNO	No	No
Electricity charges to end customers	Maybe	PNO	No	No
Emergency call handling	Yes	PNO	No	No
Emergency response	Yes	PNO	No	No
Priority services and vulnerable customers where applicable	No		No	No
UMSO where applicable	No		No	No
DCC services charges	No		No	No
Ofgem funding	No		No	No

Notes

1. How a DEH would facilitate competition in supply on a private network is outside the scope of this DCP. However, the Working Group recognises that there may be circumstances where competition in supply could be facilitated outside the settlement arrangements
2. Energisation is the logical energisation as held in the MPRS system rather than the physical Energisation on-site.
3. The term “maybe” refers to the fact that these service would only be required for customers for which supply and distribution have been unbundled and there is a non-zero distribution charge (rather than, say, a charge for network provision included in a lease’s service charge) .i.e. where the DEH has decided to apply a separate DUoS charge and has submitted a methodology to Ofgem for doing so.

Table 3 - Supply from a PNO's distribution system with a BSC MPAN (difference metering)

Service	Is it required?	Who must provide it?	Cost of service recovered as part of DNO/IDNO DUoS Charge	Charge Recovered by the PNO
Creation and maintenance of MPAN	Yes	LDNO	No	Maybe
Coordination of change of supplier process (operating the registration system (MPRS))	Yes	LDNO	No	Maybe
Energisation process (MPRS) ¹	Yes	LDNO	No	Maybe
BSC market domain data	Yes	LDNO	No	Maybe
BSC loss adjustment factors	Yes	LDNO	No	Maybe
Maintenance of agent appointments (MPRS)	Yes	LDNO	No	Maybe
DCUSA as use of system agreement	Yes	LDNO	No	Maybe
Receipt of settlement data for DUoS billing	Yes	LDNO	No	Maybe
DUoS billing and collection to Suppliers	Yes	PNO	No	Maybe
Electricity charges to end customers	Maybe	PNO	No	Maybe
Emergency call handling	Yes	LDNO	No	Maybe
Emergency response	Yes	PNO	No	Maybe
Priority services and vulnerable customers where applicable	Maybe	PNO	No	Maybe
UMSO where applicable	Maybe	LDNO	No	Maybe
DCC services charges	Yes	LDNO	No	Maybe
Ofgem funding	Yes	LDNO	No	Maybe

Notes in respect of Table 3

1. Energisation is the maintenance of the logical Energisation status as held in the MPRS system rather than the physical energisation on-site.
2. Where the LDNO provides services in respect of customers who connect to the licence exempt distribution system
3. In respect of an those MPANs that are set up for customers on the licence exempt distribution network then use of system billing would need to be provided by the LDNO in respect of each MPAN in respect of DUoS provided to the LDNO/DEH boundary. DUoS billing in respect of use of the DEH's licence exempt distribution system would only apply if the to the fact that these service would only be required where supply and distribution have been unbundled and there is a non-zero distribution charge (rather than, say, a charge for network provision included in a lease's service charge).

4. Ofgem funding and DCC charges would only be relevant if it turns out that DCC and Ofgem calculates charges to the LDNO on the basis of the number of MPANs in the DNO's MPAS, rather than the number of MPANs on the LDNO's network.
5. The Working Group assumes that the DNO could charge the supplier for services provided in table 3 above via transactional charges as detailed in the relevant charging statement.

APPENDIX 2 – Timeline

Review of the structure of charges commenced in 2000 and considered connection charge methodologies as well as those for use of system.

Prior to 2010	Use of system charges based on variants of the Boley and Fowler approach published in 1977 (use of a distribution reinforcement model)
2008	Ofgem consulted on relevant principles for UoS charging methodology
Mar 2009	Ofgem Decision on principles
Jun 2009	DNOs consult proposed CDCM <ul style="list-style-type: none"> • includes replacement costs • IDNO charges in main model (no 'Method M')
July 2009	DNOs publish revised methodology <ul style="list-style-type: none"> • excluding replacement costs • IDNO charges in main model (no 'Method M')
September 2009	DNOs publish proposals for CDCM; Ofgem publish consultation <ul style="list-style-type: none"> • excluding replacement costs • Method M introduced for IDNO Charges
December 2009	CDCM approved
April 2010	CDCM implemented
	Development of IDNO tariffs
Pre-2010	IDNOs raised concerns about DNO charging: Boundary metering required and charged to IDNOs. <ul style="list-style-type: none"> • IDNO charged as end consumers by applying HH tariffs at the site boundary • Full capacity charges levied from date of connection to network • Only large sites viable
	IDNOs engaged with DNOs raising concern that DNO approach anti-competitive <ul style="list-style-type: none"> • DNOs charged differently than they did to their own equivalent domestic customers • Charges resulted in margin squeeze • Requirement and charges for boundary meters unfair
	Ofgem encouraged DNOs to take action: <ul style="list-style-type: none"> • introduce IDNO-specific charges, and "interim" methodologies in place by April 2009 • IDNO charges to be central to the development of the CDCM
2008-09	IDNO / DNO meetings to develop IDNO charging methodologies
2009	Incremental changes to DNO charging of IDNOs: <ul style="list-style-type: none"> • Capacity ramping introduced • Charging of boundary meters removed

APPENDIX 3 – Glossary of terms

Term	Definitions from the Electricity Act are provided below
Distribute	<p>"distribute", in relation to electricity, means distribute by means of a distribution system, that is to say, a system which consists (wholly or mainly) of low voltage lines and electrical plant and is used for conveying electricity to any premises or to any other distribution system;</p> <p>Comment: The definition applies to electricity distribution systems that are licensed or operated under exemption.</p>
Electricity Distributor	<p>"electricity distributor" means any person who is authorised by a distribution licence to distribute electricity except where he is acting otherwise than for purposes connected with the carrying on of activities authorised by the licence;</p> <p>Comment: This definition excludes licence exempt distributors.</p>
Authorised Distributor	<p>"authorised distributor" means a person who is authorised by a licence or exemption to distribute electricity;</p> <p>Comment: This definition includes both licensed and licence exempt distributors.</p>
Distribution Exemption Holder	<p>"distribution exemption holder" means a person who--</p> <p>(a) is distributing electricity for the purpose mentioned in section 4(1)(bb); and</p> <p>(b) is authorised to do so by an exemption.</p> <p>Comment: The general exemptions from holding a distribution licence are contained in 2001 exemption regulations as amended.</p>

Term	DCUSA Definitions are provided below
DCUSA	Distribution Connection and Use of System Agreement - DNO Parties and IDNO Parties are required, by their licences, to be party to, comply with, and maintain this Agreement. The following definitions are contained in the relevant schedules.
DNO	Distribution Network Operator means a Party that holds a Distribution Licence in which Section B of the standard distribution licence conditions has effect, whether or not that Party is also engaged in the supply or generation of electricity. (Schedule 1A)
IDNO	Independent Distribution Network Operator means a Party that holds a Distribution Licence in which Section B of the standard distribution licence conditions does not have effect, whether or not that Party is also engaged in the supply or generation of electricity (Schedule 1A)
LDNO	Licensed Distribution Network Operator a licensed distribution network operator, meaning an IDNO Party or DNO Party operating an electricity distribution system outside of its Distribution Services Area. (Schedule 16 - CDCM)
EDNO	In Schedule 19 the term EDNO is used for portfolio billing where an “Embedded Distribution Network Operator” or “EDNO” is, in respect of each DNO Party: (a) any IDNO Party; or (b) any DNO Party acting outside of that DNO Party’s Distribution Services Area, (c) which (in each case) has a Distribution System within a GSP Group associated with that DNO Party.
	The following definitions are not contained in the DCUSA
PNO	Private Network Operators - Not defined in DCUSA. Not defined in the Electricity Act.