

Proposed variation:	Distribution Connection and Use of System Agreement (DCUSA) DCP185 – Independent Distribution Network Operator (IDNO) Discount on 20% of Residual Revenue¹		
Decision:	The Authority ² directs that proposal DCP185 be made ³		
Target audience:	DCUSA Panel, Parties to the DCUSA and other interested parties		
Date of publication:	10 September 2014	Implementation Date:	1 April 2015

Background to the modification proposal

Under the Extra-high voltage Distribution Charging Methodology (EDCM)⁴, an independent distribution network operator (IDNO) which has EDCM equivalent consumers, ie those connected at extra high voltage (EHV) but use IDNO assets, is charged by the distribution network operator (DNO) for the use of its network. The different components of this charge are calculated either according to the use of the DNO's assets by IDNO end consumers, or by using the declared boundary equivalent capacity that IDNOs have to provide, so that charges can be calculated to the boundary between the DNO and IDNO network. This includes the required network capacity (at the DNO/IDNO boundary) of each customer.

For location specific charges, where the IDNO has declared a 'boundary equivalent capacity' for a consumer, the IDNO charge is discounted by 50%. The discount is intended to reflect that IDNOs have indirect costs of their own that could displace those of the DNOs. Where the charge component is based on asset use, the IDNO is charged only for use of assets on the DNO network. The IDNO does not pay asset based charges relating to the assets that it provides to its end consumers.

As the charges set for a year do not necessarily result in the DNO receiving the allowed revenue driven by our regulatory decision in the most recent price control, the final charges are scaled up or down to make up the difference. The amount the charge is scaled by what is called the residual revenue. The residual revenue is apportioned on the basis of:

- 20% reflecting the declared capacity of consumers.
- 80% reflecting the use of assets by consumers.

At present, the 20% of residual revenue relating to capacity does not include any discount for IDNOs based on their declared boundary equivalent capacity for their consumers. In our decision on the introduction of the EDCM we suggested that industry considers applying a discount to this⁵. We noted that when residual revenue is negative, the IDNO charge would increase. We asked for a change proposal applying such a discount to consider how this can be avoided.

The modification proposal

The proposal seeks to apply a discount to location specific charges for IDNOs with EDCM equivalent consumers. The proposal is to apply a 50% discount to the 20% of residual revenue related to the declared capacity of IDNO EDCM equivalent consumers. This adjustment is intended to reflect the costs IDNOs incur when providing network services

¹ The work group uses the old term of licensed distribution network operator (LDNO) in the title of their change report, ie *LDNO Discount on 20% Residual Revenue*.

² The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably in this document. Ofgem is the Office of the Gas and Electricity Markets Authority.

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

⁴ This is one of the two common use of system charging methodologies across all DNOs. It applies to those connected to the distribution network at very high voltage levels.

⁵ Electricity distribution charging: decision on the methodology for higher voltage import charges (September 2011) <https://www.ofgem.gov.uk/ofgem-publications/43964/edcm-decision-import-charges-6-sep-2011.pdf>

to these consumers. The proposal will only apply the discount when residual revenue is positive. No adjustment would be made when residual revenue is negative.

Analysis of the changes in charges produced by this proposal, indicates that the capacity component of IDNO tariffs decreases by no more than 7%, while this component of other tariffs increases by no more than 1%.

The proposer, UKPN, believes that this change will better facilitate DCUSA Charging Objectives⁶ 3.2.1, 3.2.2 and 3.2.3. The proposer also believes that it better facilitates DCUSA General Objectives⁷ 3.1.1 and 3.1.3. The proposer states that the change proposal ensures that allocation of costs is more reflective of the costs incurred by the DNO and IDNO. Both DNOs and IDNOs will therefore be better able to comply with the obligations under their licences.

DCUSA Parties' recommendation

The Change Declaration for DCP185 indicates that all parties were eligible to vote on DCP185. In each party category where votes were cast (no votes were cast in the DG party category)⁸, there was unanimous support for the proposal and for its proposed implementation date. In accordance with the weighted voting procedure, the recommendation to us is that DCP185 is accepted. The outcome of the weighted vote is set out in the table below:

DCP185	WEIGHTED VOTING (%)							
	DNO ⁹		IDNO/OTSO ¹⁰		SUPPLIER		DG ¹¹	
	Accept	Reject	Accept	Reject	Accept	Reject	Accept	Reject
CHANGE SOLUTION	100	0	100	0	100	0	n/a	n/a
IMPLEMENTATION DATE	100	0	100	0	100	0	n/a	n/a

Our decision

We have considered the issues raised by the proposal and the Change Declaration dated 5 August 2014. We have also considered and taken into account the vote of the DCUSA Parties on the proposal, together with the Change Report, which is attached to the Change Declaration. We have concluded that:

- implementation of the change proposal DCP185 will better facilitate the achievement of the specified DCUSA Charging Objectives and General Objectives; and
- directing that the change is approved is consistent with the Authority's principal objective and statutory duties.¹²

Reasons for our decision

We consider this proposal will better facilitate DCUSA Charging Objectives 3.2.2 and 3.2.3, and has a neutral impact on the other applicable objectives. The working group

⁶ The Applicable Charging Methodology Objectives (Charging 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.
⁷ The DCUSA General Objectives (Applicable DCUSA Objectives) are set out in Standard Licence Condition 22.2 of the Electricity Distribution Licence and are also set out in Clause 3.1 of the DCUSA.

⁸ There are currently no gas supplier parties.

⁹ Distribution Network Operator

¹⁰ Independent Distribution Network Operator/Offshore Transmission System Operator

¹¹ Distributed Generation

¹² 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.

and all respondents to the consultation agree that these objectives are better facilitated by this change.

DCUSA Charging Objective 3.2.2 – 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)

The current allocation of costs between DNOs and IDNOs (and their respective consumers) could distort competition in electricity distribution. Identical consumers could face different charges depending upon whether they are connected through an IDNO or directly to the DNO network. This change will better allocate costs and thereby improve competition in electricity distribution.

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

This change will more appropriately allocate costs between DNOs and IDNOs. The allocation will be more reflective of the costs incurred by the different parties as it takes account of the IDNOs' indirect costs which can be expected to offset DNOs' indirect costs. The working group and all consultation respondents agreed with this assessment.

We note that the proposal changes the distribution of charges between consumers when residual revenue is positive. IDNO end consumers' charges fall and other consumers' charges rise. The changes in charges are small and lead to a more equitable distribution of charges.

Decision notice

In accordance with standard licence condition 22.14 of the Electricity Distribution Licence, the Authority hereby directs that modification proposal DCP185: 'IDNO Discount on 20% of Residual Revenue' be made.

Dora Guzeleva
Head of Networks Policy

Signed on behalf of the Authority and authorised for that purpose