

Proposed variation:	Distribution Connection and Use of System Agreement (DCUSA) DCP126 – Require DNOs to publish and update year-ahead forecasts of DUoS tariffs		
Decision:	The Authority ¹ directs that proposal DCP126 be made ²		
Target audience:	DCUSA Panel, Parties to the DCUSA and other interested parties		
Date of publication:	19 February 2013	Implementation Date:	1 April 2013

Background to the modification proposal

The Distribution Network Operators (DNOs) set Distribution Use of System (DUoS) charges to be paid by users of the electricity distribution networks. The DNOs are required by their licences to give us three months' notice of changes to DUoS charges and to send this information to parties (users) who are liable to pay DUoS charges.³

The DCUSA places the following requirements on DNOs when they change DUoS charges:

- Clause 19 states that the DNOs may vary their charges at any time by giving the required written notice (40 days' notice or the period specified in their Charging Statements) to users of the changes to charges. DNOs must use reasonable endeavours not to vary their charges more than twice a year and only on 1 April and 1 October each year.
- Clause 35A states that the DNOs must send data (set out in tables) of their actual/forecast revenue position for a six year period (the previous Regulatory Year⁴, the current Regulatory Year and the following four Regulatory Years) to the DCUSA secretariat (Electralink). This is to be done by the fifth working day of May, August, November and February in each year. Electralink then publishes these tables on the DCUSA website. This information provides users with the DNOs' assessment of their actual/forecast revenue position.⁵

Currently, DNOs are not required to publish and update year-ahead forecasts of DUoS tariffs. Some parties, including suppliers, have expressed concerns about volatility in network charges, including insufficient notice of changes. This uncertainty may mean that suppliers who contract with end customers build a premium into their end prices to protect themselves from this risk. Network charging volatility may also be considered as a potential barrier to entry for new suppliers.

In October 2012, we made a decision⁶ on measures to mitigate volatility in price control revenues, which are one source of volatility in network charges. We noted that the issue with volatility was not so much one of stability of network charges, but rather one of predictability. One area where improvements might be beneficial is in the provision of further information to industry. We noted that changes could be made through future price controls and through industry code arrangements to deal with the concerns raised by users. We encouraged further changes to be made to industry codes to address our conclusions.

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 Standard Licence Condition (SLC) 14 (11) of the DNO licence refers.

⁴ The term Regulatory Year is defined in Special Condition CRC2 of the electricity distribution licence.

⁵ These changes to DCUSA were introduced after our decision to approve DCUSA change proposal DCP066A 'Enhanced Provision of Cost Information' in January 2011. Our DCP066A decision appears here:

<http://www.ofgem.gov.uk/Licensing/ElecCodes/DCUSA/Changes/Documents1/DCP066D.pdf>

⁶ Our decision document is available on the Ofgem website here:

http://www.ofgem.gov.uk/Networks/Policy/Documents1/CV_Decision.pdf.

The modification proposal

DCP126 (the modification) was raised by Haven Power (the proposer) in March 2012. The modification would require DNOs to publish year-ahead forecasts of DUoS tariffs and to update these forecasts at regular intervals. The modification suggested that the timing of updates could be aligned with the cost information provided through Clause 35A, namely, in May, August, November and February each year. Where there were any significant differences from the previous update, the DNOs would be required to provide a commentary on these differences and explain these differences in a meeting with users.

The proposer considered that if the DNOs provided this illustrative information about future years' tariffs, this would give users early notice of potential changes to tariffs, and therefore improve the predictability of charges. The proposer considered that this improved certainty would facilitate competition between suppliers and also potentially reduce the risk premiums built into end customers' tariffs.

The Workgroup assessing the modification noted that illustrative DUoS tariffs would be produced from data inputs to the Common Distribution Charging Methodology (CDCM) model and the EHV Distribution Charging Methodology (EDCM) model. Of those inputs, the only ones most likely to change more than once a year were Transmission Exit Charges and Total Allowed Revenue in the CDCM model. However, the proposed solution would not preclude other input changes by DNOs.

The Workgroup had mixed views on the benefits of the modification. There was also a split in the consultation responses, between the DNOs who did not support the modification, or did not fully support the proposed solution whilst agreeing with the modification in principle, and the suppliers, who fully supported it.

The main arguments supporting the modification were that the updated tariff information produced would improve suppliers' understanding of the likely final tariffs, that all parties would have the same information produced from the same source, and that the information would complement the Clause 35A information already provided. The main arguments against the modification were that the process of producing the tariffs would be resource intensive for DNOs, there would be limited value attached to quarterly reviews, and that regular illustrative tariffs could risk confusing those using the data.

DCUSA Parties' recommendation

The majority of DNOs rejected both the modification and the proposed implementation date and suppliers unanimously supported both the modification and the proposed implementation date. In accordance with the weighted vote procedure, the industry recommendation to us is that DCP126 be rejected. The outcome of the weighted vote is set out in the table below:

DCP126	WEIGHTED VOTING (%)							
	DNO		IDNO/OTSO		SUPPLIER		DG	
	Accept	Reject	Accept	Reject	Accept	Reject	Accept	Reject
CHANGE SOLUTION	26	74	N/A	N/A	100	0	N/A	N/A
IMPLEMENTATION DATE	26	74	N/A	N/A	100	0	N/A	N/A

Our decision

We have considered the issues raised by the modification and the Change Declaration dated 15 January 2013. We have considered and taken into account the vote of the DCUSA Parties on the modification which is attached to the Change Declaration. We have concluded that:

- implementation of the change proposal DCP126 will better facilitate the achievement of the General DCUSA objectives⁷; and
- directing that the change is approved is consistent with our principal objective and statutory duties.⁸

Reasons for our decision

We have made our decision by considering the DCUSA General Objectives. We think that only DCUSA General Objective 3.1.2 is relevant for this assessment. We have not considered the modification against the DCUSA Charging Objectives as there are no changes to the common charging methodologies.

DCUSA General Objective 3.1.2 – 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

The key concerns expressed by the DNOs who did not support the modification were that:

- it would involve considerable resource on the part of DNOs to produce updates to illustrative tariffs regularly which would outweigh the benefits of producing this data; and
- it would result in updated illustrative tariffs that potentially confuse, rather than assist, users in understanding changes to tariffs.

We do not agree with these concerns. The DNOs who did not support the modification have not demonstrated in detail the resource intensive nature of the work required to produce the updated illustrative tariffs. The general view of respondents to the DCP126 consultation was that there are only two variables likely to change regularly, namely, Transmission Exit Charges and Total Allowed Revenue. In the absence of evidence that changes to these variables alone will create an excessive burden on DNOs in producing the illustrative tariffs sought, we consider that there is a benefit to producing the updated tariffs that would not be outweighed by the cost of producing them. We note that one DNO, Western Power Distribution (WPD), voted in favour of the modification at the party vote stage but did not provide reasons for the way it voted.

Similarly, there is no strong evidence that updated illustrative tariffs would confuse users. We note that the proposed legal text for the new Table 3 that will carry these data states in bold that the tariffs produced are illustrative only and do not represent the indicative or final tariffs to be applied by the relevant DNO. We also note that the modification would require DNOs to provide a written commentary, followed by a meeting with users where an oral commentary can be provided, on any changes to illustrative tariffs between updates to assist suppliers. We consider that these provisions will make it clear that the tariffs are illustrative and inform users as to the degree to which they can rely on the information.

We also note the potential benefits of the modification as set out by those who support it, namely:

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 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.

- the updated illustrative tariffs would assist market participants to improve their own forecasting of costs; and
- the potential reduction in the risk premium that users pass through to end customers due to uncertainty over charges.

We agree that the modification would have a beneficial impact on competition in the supply market. It would have the following two effects which would assist in reducing barriers to entry to the supply market:

- reduce the cashflow risks on suppliers, particularly small suppliers and those with a non-diversified customer base who are less able to manage these risks effectively; and
- reduce the need for suppliers to undertake modelling of the impact of changes to inputs to the CDCM and EDCM models themselves, which may be a complex process.

Our decision on measures to mitigate volatility in price control revenues stressed that the code processes provide the principal means for providing information to suppliers on expected changes to charges, and that DNOs have a responsibility to provide clear and robust information to users. We therefore welcome this modification as a further step in ensuring that users, in particular suppliers, are provided with information that improves their understanding of potential changes to network charges. A greater understanding of the impact of changes in tariffs will allow suppliers to take action to mitigate the impact of uncertainty in the costs that they charge to end customers. It would also assist all suppliers, not just those with a better understanding of the CDCM model, to receive illustrative tariff information in an accessible format from DNOs, enabling suppliers to compete on a more equal footing.

For these reasons, we consider the modification better facilitates the DCUSA General Objectives.

Decision notice

In accordance with standard licence condition 22.14 of the Electricity Distribution Licence, the Authority hereby directs that modification proposal DCP126 '*Require DNOs to publish and update year-ahead forecasts of DUoS tariffs*' be made.

Andrew Burgess

Associate Partner, Transmission and Distribution Policy

Signed on behalf of the Authority and authorised for that purpose