

DCUSA Consultation	At what stage is this document in the process?
<h1 data-bbox="124 376 555 465">DCP 306</h1> <h2 data-bbox="124 510 1098 645">Treatment of Ofgem Licence Fees within the PCDM</h2> <p data-bbox="108 723 826 757"><i>Raised on the 12 July 2017 as a Standard Change</i></p>	<div data-bbox="1185 365 1444 443">01 – Change Proposal</div> <div data-bbox="1185 454 1444 566">02 – Consultation</div> <div data-bbox="1185 577 1444 678">03 – Change Report</div> <div data-bbox="1185 689 1444 768">04 – Change Declaration</div>
<p data-bbox="119 813 571 846"><b>Purpose of Change Proposal:</b></p> <p data-bbox="119 869 1433 981">DCP 306 seeks to increase the cost reflectivity of the Price Control Disaggregation Model by directly allocating the Ofgem licence fee to an appropriate network tier for the calculation of the Opex allocation driver.</p> <p data-bbox="119 1003 1449 1081">This document is a Consultation issued to DCUSA Parties and any other interested Parties in accordance with Clause 11.14 of the DCUSA seeking industry views on DCP 306.</p>	
 	<p data-bbox="244 1104 1153 1137">The Workgroup recommends that this Change Proposal should:</p> <ul data-bbox="292 1137 818 1171" style="list-style-type: none"> <li>• proceed to a second Consultation</li> </ul> <p data-bbox="228 1205 1465 1305">Parties are invited to consider the questions set in section 10 and submit comments using the form attached as Attachment 1 to <a href="mailto:dcusa@electralink.co.uk">dcusa@electralink.co.uk</a> by <b>16 February 2018</b>.</p> <p data-bbox="228 1328 1281 1361">DCP 306 has been designated as a Part 1 Matter and a standard change.</p> <p data-bbox="228 1384 1353 1451">The Working Group will consider the consultation responses and determine the appropriate next steps for the progression of the Change Proposal (CP).</p>
	<p data-bbox="244 1496 699 1529">Impacted Parties: DNOs/IDNOs</p>
	<p data-bbox="244 1608 1273 1641">Impacted Clauses: Schedule XX<sup>1</sup>, Clause 6 table and a new clause 11B</p>

<sup>1</sup> Schedule XX being implemented by DCP 234 'Merging the PCDM and the extended PCDM' in April 2018

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Timetable		
The timetable for the progression of the CP is as follows:		
<b>Change Proposal timetable</b>		
<b>Change Proposal timetable:</b>		
Activity	Date	
Initial Assessment Report Approved by Panel	19 July 2017	
First Consultation issued to Parties	18 September 2017	
Methodology Pack issued to Reckon	01 November 2017	
Reckon to develop model for PCDM	16 November 2017	
Second Consultation issued to Parties	26 January 2018	
Change Report issued to Panel	11 April 2018	
Change Report issued for Voting	20 April 2018	
Party Voting Ends	11 May 2018	
Change Declaration Issued to Parties	15 May 2018	
Authority Decision	19 June 2018	
Implementation	01 April 2020	

## 1. Summary

### What?

- 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) the Authority.
- 1.2 This CP seeks to improve the cost reflectivity of Opex cost allocation within the Price Control Disaggregation Model (PCDM) (part of Schedule 16<sup>2</sup>) by allocating Ofgem licence fee costs directly to an appropriate network tier.

### Why?

- 1.3 Currently, Ofgem licence fees are calculated and paid by distributors on a £ per MPAN basis. The licence fee costs are not presently considered within the PCDM in calculating the Opex cost allocation driver. It is the view of the Proposer that the costs associated with Ofgem licence fees are not correctly allocated, leading to the Licensed Distributor Network Operator (LDNO)<sup>3</sup> tariffs being less cost reflective, particularly for Low Voltage (LV) connected end user LDNO tariffs (High Voltage (HV):LV, LV:LV etc.)

### How?

- 1.4 This change suggests that the most appropriate solution to this issue is to directly allocate the Ofgem licence fees (taken from 2007/08 Regulatory Reporting Pack table 2.6) to the LV services network level although further consideration should be given to allocating the licence fee at each network level.
- 1.5 Following the first consultation and discussion of the CP within the Working Group, the Working Group are issuing a second consultation to gain industry views on the impacts of the modelling changes that are needed to the PCDM to facilitate this change based on allocating the Ofgem licence fee to the LV service network.

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<sup>2</sup> Due to the approval of DCP 234, the PCDM will be contained in a new schedule with effect from the 1<sup>st</sup> April 2018, the number of which has yet to be allocated.

<sup>3</sup> An IDNO Party or DNO Party operating an electricity distribution system outside of its Distribution Services Area.

## 2 Governance

### Justification for Part 1 Matter

- 2.1 DCP 306 has been designated as a Part 1 Matter and therefore will go the Authority for determination after the voting period has completed.
- 2.2 This is considered a Part 1 Matter as it affects DCUSA Clause 9.4.2B and is likely to have a significant impact on competition in the distribution of electricity.

### Requested Next Steps

- 2.3 Following a review of the Consultation responses, the Working Group is proposing to progress to the Change Report phase unless feedback would suggest otherwise.

## 3 Why Change?

### Background of DCP 306

- 3.1 The Proposer suggests that the costs associated with the Ofgem licence fee are payable by all LDNOs but the derivation of the LDNO tariffs does not fully include this cost. Consequently, it is believed that LDNOs are not able to fully recover the costs incurred, or reasonably expected to be incurred in operating their distribution businesses.
- 3.2 As the Opex cost allocation driver does not take into account the Ofgem licence fee, the costs associated with the Ofgem licence fee are effectively smeared across all network levels. The resultant LDNO tariffs are not, therefore, reflective of the costs incurred by the LDNO.
- 3.3 This change proposal seeks to ensure that the LDNO tariffs better reflect the costs that are avoided by the DNO when customers are connected to their network via another LDNO.
- 3.4 The proposer suggests that by allocating the Ofgem licence fee to the LV services network level, the LDNO tariffs produced by the Common Distribution Charging Methodology (CDCM) will better reflect the mechanism by which these costs are incurred. This is consistent with the purpose of the PCDM and DCUSA Charging Objective 3.

## 4 Code Specific Matters

### Reference Documents

- 4.1 None

## 5 Working Group Assessment

### DCP 306 Working Group Assessment

- 5.1 The DCUSA Panel established a Working Group to assess DCP 306. This Working Group consists of Distribution Network Operator (DNO) and Independent Distribution Network Operator (IDNO) representatives and an Ofgem observer. Meetings were held in open session and the minutes and papers of each meeting are available on the DCUSA website – [www.dcusa.co.uk](http://www.dcusa.co.uk).
- 5.2 The rationale for this CP being raised is because currently the Ofgem licence fees form part of residual charges when calculating the CDCM tariffs and as such is not a separate cost element within the PCDM. This change will be looking to review the impacts of changing this i.e. allocating the licence fee either by, as the Proposer suggest, a 100% allocation to the LV service level or alternatively allocated across each voltage level within the PCDM. All other aspects of Opex would be unchanged.
- 5.3 The Working Group considered how the licence fee is currently derived and then subsequently allocated with the CDCM. It was determined that Ofgem charge each DNO a licence fee on a £/MPAN basis. This is then recovered as part of the residual charging calculation when deriving the all the way tariffs in the CDCM. It was confirmed that since the change is in the PCDM there would be no impact on the all the way tariffs and as such no impact on end customers connected directly to the host DNO network, other than any resulting indirect impact on the recovery of the residual charge.
- 5.4 The Working Group considered whether a more appropriate change would be to the CDCM by taking the licence fee out of residual charges and within the methodology itself. This was discounted since it would not align with the intent.
- 5.5 The timing of the change was questioned as, on 4 August 2017 Ofgem launched a Targeted Charging Review (TCR) Significant Code Review (SCR). One of the key areas within the TCR covers residual charging. It was discussed whether it would be more practicable to progress the proposed change as part of the wider CDCM review or as part of the TCR.
- 5.6 It was decided that as the change is specifically looking at the PCDM, the Working Group would not be able to include CDCM or EHV Distribution Charging Model (EDCM) amendments in their solutions as it would change the intent of the proposal. Therefore, there shouldn't be any impact on the TCR.
- 5.7 The Working Group then considered whether the allocation within the PCDM should only be applied to the LV network level and whether it may be even more cost reflective if the allocation of the licence fee was placed against each network level. The Working Group agreed to seek the views of Parties on this matter to define the solution.
- 5.8 The Proposer is suggesting that the costs described in table 2.6 of the 2007/2008 Regulatory Reporting Pack (RRP) as "Ofgem licence fees" be used. The reasoning for this is that it matches the rest of the data source being used within the PCDM. A counter argument was that it may be more cost reflect to use the latest licence fee costs rather than the ones that are ten years old. The Working Group were of the view that for consistency the 2007/2008 RRP should be used as it aligns with how the rest of the operational costs have been allocated within the PCDM.
- 5.9 The Working Group sought industry views in the first consultation on:
- Whether the TCR or CDCM review work is a more appropriate work stream to review this issue;
  - Is it more appropriate to allocate the licence fee at each voltage level or just at the LV network level, and if so is the data on customer numbers at each voltage level easily identified.; and

- Is the 2007/08 data the best data set to use or is there a better data source that could be utilised?

## First Consultation

- 5.10 To aid the further development of the solution for this CP, the Working Group issued a consultation to Parties on 18 September 2017. The aim of the first consultation was to ask the industry for their views on the principles of the change. There were six responses to the first consultation comprising of four DNOs and two IDNOs. A copy of the first consultation as well as a summary of the consultation responses and the Working Group conclusions can be found as Attachment 2.
- 5.11 All respondents agreed that they understood and agreed with the principles and intent of the change. However, one DNO respondent highlighted that they did not agree with how the Proposer suggests that the Ofgem licence fees for a DNO are determined by MPANs. The Working Group accepted the comments made by the DNO on how the costs are produced by Ofgem, however, the CP is looking at allocating the Ofgem licence fees on a £/MPAN basis which is moving from a fixed cost to unit cost method and is not a like for like for what currently happens. Although the Working Group acknowledged the comments made by the respondents, they still wish to continue with the original principles of the change as they believe the solution will provide better cost reflectivity.
- 5.12 Respondents to the first consultation highlighted that the Working Group would need to be cautious about the outputs from Ofgem's Charging Future's Forum (CFF) and their subsequent Task Forces that have been organised. The Working Group recognise that the change is in the gift of the Proposer and unless directed otherwise by the Authority the CP will progress since the change impacts the PCDM and not the CDCM.
- 5.13 The first consultation also sought industry views on how the Ofgem licence fees should be allocated with the PCDM and whether it should be at LV voltage level or be allocated at each voltage level based on the number of customers connected at each. The majority of Parties that responded to the consultation wanted to allocate the Ofgem licence fees at various voltage levels.
- 5.14 All respondents to the first consultation believed that the 2007/08 data set was the best data set to use for this change as it would be consistent with the rest of the PCDM. However, it was highlighted that the industry may need to consider a wider review in the future.

## Working Group Conclusions and next steps

- 5.15 The Working Group identified two areas of further work having discussed the Parties' responses to the first two items within the consultation identified under paragraph 5.9 above:
- Review the papers submitted to the CFF which were distributed since the first consultation; and
  - Identify the number of customers at each voltage level in order to determine whether it is more appropriate to allocate the LV licence fee at each voltage level or just at the LV network level.
- 5.16 The Working Group agreed with the Parties' response to the third item in Para 5.9 above relating to the use of 2007/08 data.
- 5.17 On the first area of further work, Ofgem issued two papers in advance of the CFF:
- [Targeted Charging Review working paper](#), and
  - [Reform of electricity network access and forward-looking charges](#).

The Working Group reviewed both papers. This is discussed further under section 8 below

5.18 On the second area, Parties supported the allocation of the licence fee at each voltage level from a cost reflectivity perspective. In order to develop this, the Working Group requested from the DNO community the number of customers at each voltage level. When this was analysed there were 99.8% of customers forecast to be connected at the LV network level. The Working Group concluded that from a pragmatic point of view it may be sensible to allocate at the LV network level rather than at each voltage level. This would reduce cost reflectivity (but likely to be immaterial) but improve simplicity.

## Second Consultation

5.19 Following on from the responses of the first consultation and the analysis undertaken, under paragraph 5.18, the Working Group agreed that the Ofgem licence fees should be allocated to LV voltage level customers rather than at each voltage level. The rationale for this decision is based on the fact that >99% of customers are connected at this voltage level and so would provide a more simplified solution at the expense of a minimal improvement in cost reflectivity.

5.20 The Working Group are seeking views on the rationale used to determine that the licence fees should only be allocated at the LV network level (since the view of Parties was that it should be at each voltage level). The Working Group would like Parties to consider this in light of the impact on LDNO tariffs in section 8 below.

**Q1: Are Parties comfortable with the approach proposed by the Working Group to allocate the Ofgem licence fees to the LV Service Customers rather than allocating them across all voltage levels? If not provide your rationale.**

## 6 Legal Text

6.1 The draft legal text acts as Attachment 3 to this consultation.

6.2 The draft legal text amends Schedule XX, Clause 6 table and a new clause 11B, which is being implemented by DCP 234 'Merging the PCDM and the extended PCDM'

6.3 The legal text will be updated as follows:

**Table: Allocation rules**

Non activity costs and reconciling amounts	<del>Do not allocate</del> see paragraph 11A in this schedule XX		<u>see paragraph 11A in this schedule XX+</u>
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**11A** RRP costs described in the table at 6 above as "Non activity costs and reconciling amounts" shall be allocated as follows:

- (a) Costs described in table 2.6 of the 2007/2008 RRP as "Ofgem licence fees" shall be 100% allocated directly to the LV services level and treated as indirect costs.
- (b) No other costs shall be directly allocated

6.4 The Working Group would like industry feedback on the proposed legal text.

**Q2 Do you have any comments on the proposed legal text?**

## 7 Relevant Objectives

### Assessment Against the DCUSA Objectives

- 7.1 For a DCUSA Change Proposal to be approved it must be demonstrated that it better meets the DCUSA Objectives. Following on from the first consultation, respondents agreed with the Proposer that DCUSA Charging Objective 3 would be better facilitated as the LDNO tariffs produced by the CDCM will better reflect the mechanism by which the costs are incurred.
- 7.2 The Working Group have concluded that they are minded to adopt the approach of allocating the Ofgem licence fees to LV network customers rather than customers at each voltage level, therefore, the Working Group seeks industry opinion on whether DCUSA Charging Objective 3 would still be positively impacted by the change and whether any of the other DCUSA Charging would be better facilitated.

**Q3: Which of the DCUSA Charging Objectives are better facilitated by this change? Please provide your rationale.**

DCUSA Charging Objectives:
<p><b>Charging Objective 1</b> – 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</p>
<p><b>Charging Objective 2</b> – 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)</p>
<p><b>Charging Objective 3</b> - 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</p>
<p><b>Charging Objective 4</b> - 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</p>

**Charging Objective 5** - that compliance by each DNO Party with the Charging Methodologies facilitates compliance with the Regulation on Cross-Border Exchange in Electricity and any relevant legally binding decisions of the European Commission and/or the Agency for the Co-operation of Energy Regulators.

**Charging Objective 6** - that compliance with the Charging Methodologies promotes efficiency in its own implementation and administration.

## 8 Impacts & Other Considerations

### Does this Change Proposal impact a Significant Code Review (SCR) or other significant industry change projects, if so, how?

- 8.1 The Working Group discussed whether it would be better if the intent of this change is reviewed as part of Ofgem's TCR or the wider CDCM review. Ofgem provided two papers for the Working Group to review and decide whether the change is under the Working Group's remit or whether they should be considered by the TCR or the CFF and one of its Task Forces.
- 8.2 The Working Group highlighted that the TCR is reviewing residual charges, while the Task Forces will be covering forward-looking charges and access arrangements. As the Working Group are solely focussing on the PCDM, there is no direct interaction between this proposal and the TCR. Therefore, unless the Working Group are given direction by Ofgem to put the proposal on hold, they are going to continue to discuss the solution.
- 8.3 The Ofgem representative highlighted that the proposal could eventually be covered by the Task Forces and any changes as a result of this proposal could be superseded by the outcomes of the Task Forces at a later date. This was noted by the Working Group.

**Q4: Do you agree that the change should continue to be assessed via the DCUSA Change Process and not the SCR, CFF or wider Task Forces?**

### Consumer Impacts

- 8.4 The Working Group requested that the DCUSA Modeller conduct an update on the PCDM to reflect the impacts on the consumer and LDNO tariffs when allocating the Ofgem licence fees to LV voltage level customers (Attachment 4).
- 8.5 The impact assessment on the end user tariffs showed that there was a positive difference of between +0.01% and +0.17% on the Unit Rate 1 (p/kWh) tariffs for all DNO areas. There was also a small difference between +0.01% and +0.18% for the fixed charge for some of the DNO areas.
- 8.6 The Working Group also noted that the impact assessment on the LDNO tariffs showed that there were both positive and negative effects on all DNO areas when allocating the Ofgem licence fees to LV service level customers.

- 8.7 These effects ranged from -2.38% to +1.41% on the unit rate 1 (p/kWh) tariffs for all DNO areas and -3.70% to +1.16% on the fixed charge tariffs for all DNO area when allocating the Ofgem licence fees to LV service level customers.
- 8.8 The following outcomes also came from the modelling update:
- DCP 306 would increase discount percentages for LV end-user demand, and reduce (or leave unchanged) discount percentages in all other cases.
  - The largest impact is on discount percentages for LV-end user demand with a LV LDNO boundary. For this configuration, the increase in discount percentages caused by DCP 306 would range from 0.22 percentage points to 0.51 percentage points.
  - For LV end-user demand with a HV or HV plus LDNO boundary, the increase in discount percentages caused by DCP 306 would range from 0.05 percentage points to 0.31 percentage points.
  - The largest reduction in discount percentages caused by DCP 306 is 0.12 percentage points this is for HV end user demand with a HV plus LDNO boundary in the Northern Powergrid Northeast area.
  - There are some small increases (up to 0.27 percent) to CDCM end user tariffs in all DNO areas.
- 8.9 In summary, the majority of the end user tariffs are unaltered, and those that are, in the main result in 0.01p/kwh increase in the unit rate and a 0.001p/MPAN/day increase in the fixed charged rate. The full impact assessment can be found in Attachment 4.

## Environmental Impacts

- 8.10 In accordance with DCUSA Clause 11.14.6, the Working Group assessed whether there would be a material impact on greenhouse gas emissions if this CP was implemented. The Working Group did not identify any material impact on greenhouse gas emissions from the implementation of this CP.

## Engagement with the Authority

- 8.11 Ofgem has been fully engaged throughout the development of this CP as an observer on the Working Group.

**Q5: Do you have any further comments for the Working Group?**

## 9 Implementation

- 9.1 The original proposed implementation date for this CP was 01 April 2019. However, on further reflection the Working Group agreed that this could be too ambitious and agreed that the implementation date would be more feasible on 01 April 2020.
- 9.2 Respondents to the first consultation agreed that an implementation date of 01 April 2020 would be the most feasible date, and as such is the date the Working Group are proposing.

## 10 Consultation Questions

10.1 The Working Group is seeking industry views on the following consultation questions:

Number	Questions
1	Are Parties comfortable with the approach proposed by the Working Group to allocate the Ofgem licence fees to the LV Service Customers rather than allocating them across all voltage levels? If not, provide your rationale.
2	Do you have any comments on the proposed legal text?
3	Which of the DCUSA Charging Objectives are better facilitated by this change? Please provide your rationale.
4	Do you agree that the change should continue to be assessed via the DCUSA Change Process and not the SCR, CFF or wider Task Forces?
5	Do you have any other comments for the Working Group?

10.2 Responses should be submitted using Attachment 1 to [dcusa@electralink.co.uk](mailto:dcusa@electralink.co.uk) no later than **16 February 2018**.

10.3 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.

### Attachments

- Attachment 1 - DCUSA Consultation Response form
- Attachment 2 – DCP 306 Consultation 1
- Attachment 3 – DCP 306 Proposed Legal text
- Attachment 4 – DCP 306 PCDM model and impact assessment