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DCUSA Consultation

DCP097 Changes to the method of cost allocation employed in the Price Control Disaggregation Model for DNO indirect cost categories specifically associated with the volume of customers using the DNO network.

PURPOSE

- 1.1 The Distribution Connection and Use of System Agreement (DCUSA) is a multi-party contract between electricity Distributors, 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 document is a consultation issued to DCUSA Distributor and Supplier Parties and to all other interested parties in accordance with Clause 11.14 of the DCUSA seeking views on the implementation of DCUSA CP 097¹ entitled *"Changes to the method of cost allocation employed in the Price Control Disaggregation Model for DNO indirect categories specifically associate with the volume of customers using the DNO network"*. This proposal seeks to change the methodology for the calculation of the LDNO discounts, which are in turn used to determine portfolio tariffs applied in respect of LDNO networks connecting to a DNO's distribution system.
- 1.3 Parties are invited to consider the following:
- 1.3.1 The impact assessment carried out by the Working Group as set out in section 2.4, and associated analysis in Appendix A, and
 - 1.3.2 The proposed legal drafting changes to Schedule 16 of the DCUSA as set out in section 5, and
 - 1.3.3 The Working Groups evaluation of DCP094 against the DCUSA and Charging objectives as set out in section 6, and
 - 1.3.4 The consultation questions listed in section 8.
- 1.4 Parties should submit comments using the consultation response form attached as Appendix C - DCP097 Response Form
- 1.5
- 1.6 should be sent to dcusa@electralink.co.uk by no later **than 12 pm on 2 September 2011**.

¹ <http://www.dcusa.co.uk/Extranet/CP.aspx?id=114>

2 SUMMARY

- 2.1 The CDCM calculates portfolio tariffs for LDNO networks that connect to a DNO's distribution system by applying LDNO discounts to final tariffs (i.e. tariffs calculated in respect of end consumers on the DNO Party's network). Step 4 of Schedule 16 in DCUSA describes the principles that the CDCM employs to calculate LDNO discounts. In practice these principles are embedded in an Excel workbook entitled "Method M". In calculating the LDNO discounts the methodology allocates certain (but not all) DNO indirect opex costs to different network levels using different cost drivers. (RRP data already allocates direct costs to the relevant network level). It then calculates weighted average percentages for allocating the DNO opex costs. In practice the weighted average percentages are calculated in the Method M '*WPD – Opex Allocation*' worksheet and used to allocate opex costs in the Method M '*WPD- Final Allocation*' worksheet. . In addition, the proportion of direct costs to indirect costs is used in the calculation of LDNO discounts where the LDNO connects to the DNO within a network level; for instance, where an LDNO connects to the upstream distributor at LV and where the downstream customer is connected at LV.
- 2.2 Currently some of the indirect operating costs are allocated to each network level using an estimate of the percentage of the total modern equivalent asset value provided at each network level. of the DNO's distribution system as a cost driver. Not all indirect costs are allocated to network levels; where they are not allocated they do not play a part in determining the weighted average percentage used to allocate operating costs.
- 2.3 **The intent** of DCP097 is to change the cost drivers used to allocate some of the indirect costs. The proposed changes to the cost drivers are shown below:

Cost Category	Cost Allocation Driver	
	Current	Proposed
Customer Call Centre	MEAV	No Customers
IT & Telecoms	Do Not Allocate	MEAV /Customer Numbers*
Property Mgt	Do Not Allocate	MEAV /Customer Numbers*
HR & Non-operational Training	MEAV	No Customers
Finance & Regulation	MEAV	No Customers
CEO etc	MEAV	No Customers

* The change proposal notes that the *IT/Telecoms* and *Property Management* costs should be allocated. By allocating more of the indirect costs, direct costs do not have an undue bearing on the weighted average percentage of costs used to allocate opex. To that extent the proposer believes that using either MEAV or Customer Numbers better facilitated the DCUSA objectives compared to not allocating such costs. The proposer felt that the case for using customer numbers as a cost driver for these two costs types was less clear and that there was also a case for using MEAV to allocate such costs

- 2.4 The justification for the change of cost drivers for: *Customer Call Centre, HR and Non-Operational Training, Finance and Regulation, and CEO etc*, was that use of modern equivalent asset values (MEAV) was an inappropriate cost driver for these indirect costs and that using '*No of customers*' as a cost driver better reflected the way these indirect costs were incurred.

3 IMPACT ASSESSMENT OF DCP094

- 3.1 To enable the Working Group to complete its impact assessment of DCP097 a request for information (RFI) was issued to the DNOs on the 5th August 2011.
- 3.2 The RFI requested DNOs to assess the impact that the change proposal DCP094 would have on the LDNO discounts used in the October 2011 version of the CDCM (i.e. taking the implementation of DCP-71A into account). To facilitate this impact assessment the RFI identified changes that would need to be made to the October 2011 version of their Method M model(s). The specification provided in the RFI for changes to the Model M was based on the method employed when the original draft of DCP097 was submitted to the DCUSA secretariat for initial assessment.
- 3.3 The RFI requested that DNOs propose alternative ways to meet the intent of DCP097 where they felt it was appropriate. The RFI also specified the format in which the data required by the Working Group was to be returned.
- 3.4 The data returned by DNOs was anonymised by the DCUSA Secretariat prior to analysis by the Working Group, and consisted of updates to LDNO discount tariffs and Supplier tariff information as shown in tables 1037 and 3701 of the Method M model, respectively. The data is attached in Appendix A - DCP097 Anonymised Impact Analysis returned by DNOs

3.5 The results of the LDNO discount tariffs (CDCM Table 1037) are summarised as follows:

3.5.1 Changes to Discount factors using cost drivers specified in paragraph 3.7 of RFI are illustrated below. Changes to Cost Driver are as follows:

Cost Category	Cost Allocation Driver	
	from	To
Customer Call Centre	MEAV	No Customers
IT & Telecoms	Do Not Allocate	MEAV
Property Mgt	Do Not Allocate	MEAV
HR & Non-operational Training	MEAV	No Customers
Finance & Regulation	MEAV	No Customers
CEO etc	MEAV	No Customers

3.5.2 Results of DNOs impact assessments are as follows:

	LDNO Discounts under DCP097				Difference from October 2011 LDNO Discount			
	LDNO LV: LV user	LDNO HV: LV user	LDNO HV: LV sub user	LDNO HV: HV user	LDNO LV: LV user	LDNO HV: LV user	LDNO HV: LV sub user	LDNO HV: HV user
DNO 1	36.1%	63.7%	41.0%	30.9%	1.9%	0.9%	0.0%	0.1%
DNO 2	32.2%	65.2%	46.7%	37.1%	3.4%	1.5%	-0.1%	-0.1%
DNO 3	33.4%	57.0%	33.2%	22.4%	3.1%	1.8%	0.1%	0.2%
DNO 4	32.7%	65.6%	45.8%	39.1%	2.3%	0.9%	0.0%	0.1%
DNO 5	31.9%	59.9%	37.4%	30.8%	2.9%	1.4%	0.0%	0.1%
DNO 6	23.2%	47.2%	27.8%	19.6%	2.6%	2.8%	1.8%	2.1%
DNO 7	30.6%	55.8%	33.4%	26.0%	2.6%	1.3%	-0.2%	-0.1%
DNO 8	29.4%	51.0%	27.3%	19.1%	2.0%	1.0%	-0.2%	-0.2%
DNO 9	30.8%	52.0%	27.6%	18.3%	2.1%	1.1%	-0.2%	0.0%
DNO 10	28.8%	49.8%	27.9%	19.3%	1.9%	1.1%	-0.2%	0.0%
DNO 11	34.9%	62.4%	39.7%	26.1%	1.8%	0.9%	-0.1%	-0.1%
DNO 12	33.2%	63.9%	40.9%	28.8%	2.5%	0.9%	-0.2%	-0.3%
DNO 13	33.4%	57.8%	35.5%	27.3%	1.9%	0.8%	-0.4%	-0.4%
DNO 14	27.3%	59.2%	43.5%	38.9%	2.5%	1.4%	0.2%	0.4%

3.5.3 Changes to Discount factors using cost drivers specified in paragraph 3.8 of RFI:

Cost Category	Cost Allocation Driver	
	from	To
Customer Call Centre	MEAV	No Customers
IT & Telecoms	Do Not Allocate	Customer Numbers
Property Mgt	Do Not Allocate	Customer Numbers
HR & Non-operational Training	MEAV	No Customers
Finance & Regulation	MEAV	No Customers
CEO etc	MEAV	No Customers

3.5.4 Results of DNOs impact assessments are as follows:

	Discount factors under DCP096				Difference from Current LDNO Discount			
	LDNO LV: LV user	LDNO HV: LV user	LDNO HV: LV sub user	LDNO HV: HV user	LDNO LV: LV user	LDNO HV: LV user	LDNO HV: LV sub user	LDNO HV: HV user
DNO 1								
DNO 2	34.8%	65.7%	45.5%	35.6%	6.0%	2.0%	-1.3%	-1.5%
DNO 3	36.3%	58.3%	32.2%	21.3%	6.1%	3.1%	-0.8%	-0.9%
DNO 4	34.2%	65.7%	44.6%	37.9%	3.8%	1.0%	-1.1%	-1.1%
DNO 5	34.0%	60.5%	36.4%	29.9%	5.0%	2.0%	-1.0%	-0.8%
DNO 6								
DNO 7								
DNO 8								
DNO 9	32.9%	53.3%	27.3%	17.9%	4.3%	2.3%	-0.5%	-0.4%
DNO 10	30.8%	51.1%	27.8%	19.1%	3.9%	2.4%	-0.3%	-0.2%
DNO 11	36.1%	62.7%	39.1%	25.5%	3.0%	1.2%	-0.6%	-0.7%
DNO 12	34.7%	64.1%	39.9%	27.6%	4.1%	1.1%	-1.2%	-1.5%
DNO 13	34.6%	58.0%	34.8%	26.6%	3.0%	1.1%	-1.2%	-1.1%
DNO 14	29.8%	59.3%	41.5%	37.0%	5.0%	1.5%	-1.8%	-1.5%

- 3.6 The impact on Supplier tariffs was analysed by DNOs; the Working Group's view was that the absolute impacts were small or negligible in all cases. These impacts are shown in Appendix A.
- 3.7 This Consultation seeks confirmation from respondents on that Working Group Assessment is correct.

4 ALTERNATIVE OPTIONS TO THE MEET THE INTENT OF DCP 094

- 4.1 The Working Group considered there were no alternative options available to meet the intent of DCP097. Furthermore, no alternative options were put forward by any DNOs in their response to the RFI.

5 PROPOSED AMENDMENT AND LEGAL DRAFTING

- 5.1 The proposed legal drafting of DCP 097 has been drafted by the Working Group and is as follows:

- 5.1.1 The DCUSA Panel has identified that the Model M workbook does not come under the governance of DCUSA. Therefore, it is proposed that the cost drivers for each indirect cost category are specified in Schedule 16. The Changes to Schedule 16 of the DCUSA are as follows:

Paragraph 102 change to read as follows:

~~"Indirect operating costs are allocated to network levels on the basis of an estimate of modern equivalent asset value by network level using cost drivers specified below. The operating cost percentage for each network level is a weighted average of the direct and indirect percentages. Estimated gross modern equivalent asset values used for this purpose are derived from asset counts and gross modern equivalent asset values (replacement costs) for various asset types."~~

Cost Description	Driver type
Network Policy	MEAV
Network Design & Engineering	MEAV
Project Management	MEAV
Engineering Mgt & Clerical Support	MEAV
Control Centre	MEAV
System Mapping - Cartographical	MEAV
Customer Call Centre	Customer numbers
Stores	MEAV
Vehicles & Transport	MEAV
IT & Telecoms	MEAV/ Customer numbers
Property Mgt	MEAV/ Customer numbers
HR & Non-operational Training	Customer numbers
Health & Safety & Operational Training	MEAV
Finance & Regulation	Customer numbers
CEO etc	Customer numbers
Atypical cash costs	Do not allocate
Pension deficit payments	Do not allocate
Metering	Do not allocate
Excluded services & de minimis	Do not allocate
Relevant distributed generation (less contributions)	Do not allocate
IFI	Do not allocate
Disallowed Related Party Margins	Do not allocate
Statutory Depreciation	Do not allocate
Network Rates	Do not allocate
Transmission Exit Charges	EHV only
Pension deficit repair payments by related parties (note	Do not allocate
Non activity costs and reconciling amounts (note 3)	Do not allocate

Where:

the modern equivalent asset values used for this purpose are derived from asset counts and gross modern equivalent asset values (replacement costs) for various asset types; and

customer numbers are the number of MPANs connected at each network level.

The weighted average percentage is then used to allocate the total operating cost identified for DPCR4 to network levels."

5.2 The Working Group recommends implementation on 1st April 2012.

6 EVALUATION AGAINST THE DCUSA AND CHARGING OBJECTIVES

6.1 The Working Group considers that DCP 097 has an impact the following DCUSA objective:

6.1.1 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.

6.1.2 DNO indirect costs are not considered to be closely linked to assets. This point was made in DNOs' submission of the EDCM. The Working Group considers that Objective 3.1.2 will be better facilitated by DCP097 since it considers that the proposed cost drivers offer a better proxy than modern equivalent asset values for allocating the indirect costs and thus better promote competition in distribution.

6.2 The Working Group considers that DCP 097 will have an impact on the following Charging Methodologies objectives:

6.2.1 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);

6.2.2 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;

6.3 The Working Group considers that under DCP 097 Objective 3.2.2 will be better facilitated as the CPs will increase cost reflectivity and thus reduce distortion in the distribution of electricity, as detailed in 6.2.

- 6.4 The Working Group considers that under DCP 097 Objective 3.2.3 will be better facilitated as the CP will improve cost reflectivity, as detailed in section 6.2.

7 IMPLEMENTATION

- 7.1 The Working Group recommends, subject to Authority approval, implementation from 1 November 2011 with revised charges to be reflected in tariffs taking effect from 1 April 2012. In light of the next steps set out in section 9, the outcome of DCP097 will be known by November 2011, allowing Distributors to take the proposal into account when publishing their indicative charges in December 2011 and final prices in February 2012 for implementation from 1 April 2012.

8 CONSULTATION

- 8.1 This consultation seeks views from DCUSA Distributor and Supplier Parties, and all interested parties on the following questions.
- 8.1.1 Do you understand the intent of DCP097 and are you supportive of its principles?
- 8.1.2 Do you agree with the Impact Analysis undertaken by DNOs on behalf of the Working Group?
- 8.1.3 Do you agree with the associated impact assessment completed by the Working Group?
- 8.1.4 Do you agree that the legal drafting in section 5 is appropriate to meet the Intent of DCP 097?
- 8.1.5 For IT & Telecoms and for Property Management which driver do you think should be used; MEAV or Customer Numbers? Please provide supporting comments
- 8.1.6 Do you agree with the Working Group's assessment that DCP097 better meets the DCUSA General and Charging objectives as outlined in section 6? if not, please explain why and provide your assessment against the objectives.

8.1.7 Do you believe that the intent of DCP097 is adequately met or that there are alternative ways of meeting the intent of DCP097?

8.1.8 Please state any other comments or views on the Change Proposal?

8.2 Responses should be submitted using Appendix C to dcusa@electralink.co.uk no later than **12 pm on 2 September 2011**.

8.3 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.

9 NEXT STEPS

9.1 Following the end of the consultation period the responses will be considered by the Working Group in preparation of their final report and recommendation to the DCUSA Panel. The Change Proposal will then be issued to the DCUSA panel for voting and following the vote will be issued to Ofgem for final determination.

9.2 If you have any questions about this paper or the DCUSA Change Process please contact the DCUSA Help Desk by email to DCUSA@electralink.co.uk or telephone 020 7432 3011.

10 APPENDICES

Appendix A - DCP097 Anonymised Impact Analysis returned by DNOs

Appendix B - Working Group Request for Information (RFI) to DNOs to analyze the impact of DCP097

Appendix C - DCP097 Response Form