DCUSA

DCUSA Change Proposal (DCP)	At what stage is this document in the process?

DCP 423:

LDNO Discounts for negative scaling

Date Raised: 9th May 2023

Proposer Name: Tom Cadge

Company Name: The Electricity Network Company

Party Category: IDNO

01 – Change Proposal
02 – Consultation
03 – Change Report
04 – Change Declaration

Purpose of Change Proposal:

The purpose of this change proposal is to set a floor on the LDNO discount applied to negative tariff components, after scaling, for demand tariffs. The intent of this change proposal is to seek to remedy what the proposer believes is an unintended outcome of the implementation of Ofgem's Targeted Charging Review where LDNO tariffs can be higher than the equivalent all-the-way tariff i.e. the LDNO margin is negative for that component.

Governance:

The Proposer recommends that this Change Proposal should be:

- Treated as a Part 1 Matter;
- Treated as a Standard Change; and
- Progressed to the Working Group phase.

The Panel will consider the proposer's recommendation and determine the appropriate route.

Impacted Parties: DNOs/IDNOs

Impacted Clauses: Schedule 16

Contents

Indicative Timeline

The Secretariat recommends the following timetable:	
Initial Assessment Report	17 May 2023
Consultation Issued to Industry Participants	TBC
Change Report Approved by Panel	15 November 2023
Change Report issued for Voting	17 November 2023
Party Voting Closes	08 December 2023
Change Declaration Issued to Parties	12 December 2023
Change Declaration Issued to Authority	12 December 2023
Authority Decision	TBC

Any questions?

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1 Summary

What?

1.1 Ofgem's Targeted Charging Review changed the way that residual revenue (i.e. the difference between modelled tariffs and total revenue) was recovered in use of system tariffs. The changes implemented under DCP 361 (Ofgem Targeted Charging Review Implementation: Calculation of Charges) moved the allocation of the residual revenue from being part of the unit rates to being part of the fixed charge. One of the outcomes of DCP361 was to floor the fixed charge to 0p/MPAN/year where the residual component is negative and allocating to the fixed charge would otherwise have led to a negative fixed charge. The remainder of the negative residual is then taken from Green, Amber and Red unit rates.

1.2 As part of ensuring that the fixed charge does not go negative, the CDCM takes into consideration pass-through items which are also recovered as a fixed charge adder but not modelled in the CDCM (SoLR and bad debt costs). LDNO tariffs are set based on 'discounts' which are calculated in accordance with Schedule 29 of the DCUSA. These discounts are represented as a % of the tariff which is, ordinarily, designed to be applied uniformly across all tariff components. The discount % are not applied to the pass-through elements of the fixed charge to ensure that LDNOs do not receive a margin on these elements.

1.3 The unintended outcome of considering the pass-through items in determining the maximum negative residual component but separating these out for the application of the LDNO discount to the fixed charge is that the LDNO discount is capable of being applied to negative fixed charges. When this happens the charge to the LDNO becomes a more valuable (less negative) number and when the pass-through elements are then added to the discounted rate it means that the LDNO fixed charge is higher than the all-the-way equivalent. This results in the scenario where the LDNO is charged more than the upstream DNO for a like-for-like connection tariff under CDCM, but not recoverable from the supplier.

Why?

1.4 It is the proposers belief that this is an unintended outcome of both the introduction of the TCR and also the work to recover pass through items as distinct, fixed charge elements (see DCPs 332 and 333) that LDNO tariffs can be in excess of tariffs which LDNOs can charge to suppliers.

1.5 It is recognised that there are other elements of the tariffs where the LDNO tariff is lower than the all-the-way equivalent and the LDNO will earn a margin in these areas reflective of the discount calculated in Schedule 29. However, the current application of the pass through and scaling creates a situation where this margin is altered without economic justification. Although it requires a specific set of circumstances for this situation to arise (for there to be sufficient negative scaling for the fixed charge to become floored at zero , and also for there to be bad debt or SoLR costs recovered in that year), it has been observed in the 2023-24 tariffs for UKPN's London region.

1.6 The scale of the issue is not necessarily limited as the size of the negative margin on the fixed charge component is dependent on the size of the pass through and the potential size of the negative scaling factor.

How?

1.7 It is proposed that an additional step is put into the CDCM to not apply LDNO discount percentages, as calculated in Schedule 29, to tariff components where the tariff component calculated after scaling has been applied but before fixed adders have been applied, is negative. This will ensure that no negative margins are observed for any tariff component for LDNOs.

2 Governance

Justification for Part 1 and Part 2 Matter

2.1 This change proposal is seeking to remedy the adverse outcome that the current application of scaling and pass through costs is having on LDNOs where there is negative margins available in fixed charges in certain circumstances. Although this may have a limited impact on competition at present with the current published charges, it is possible that this may manifest in greater disparity in the future if left unresolved.

Requested Next Steps

2.2 This Change Proposal should:

- Be treated as a Part 1 Matter;
- Be treated as a Standard Change; and
- Proceed to the Working Group phase.

3 Why Change?

3.1 As set out in Section 1 of this change proposal form it is the proposer's belief that there is no sound economic reason for LDNOs to receive negative margins for connections to their networks and this is possible, and real, through the CDCM as it is implemented today.

3.2 This outcome is an unintended, and unforeseen consequence of the implementation of previous work on DUoS charges which, for the reasons, set out above should be remedied for future tariffs.

4 Solution and Legal Text

Legal Text

4.1 Schedule 16 – Paragraph 98

For demand users, the discount percentages are applied to all components in all-the-way tariffs, except for instances where they would be applied to tariff components below zero, in order to determine embedded network portfolio tariffs. Where they would be applied to tariff components below zero, no discount is applied.

Text Commentary

4.2 This addition to the legal text is intended to put in place a simple fix where no discount is applied to tariffs less than zero. By not applying this step to those tariffs, there will be no opportunity for the margin to be negative on any tariff component.

5 Code Specific Matters

Reference Documents

5.1 None

6 Relevant Objectives

	DCUSA Charging Objectives	Identified impact
☑	1. 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	Positive
☑	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)	Positive
☑	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	Positive
☐	4. 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	None
☐	5. That compliance by each DNO Party with the Charging Methodologies facilitates compliance with the EU Internal Market Regulation and any relevant legally binding decisions of the European Commission and/or the Agency for the Co-operation of Energy Regulators; and	None
☐	6. That compliance with the Charging Methodologies promotes efficiency in its own implementation and administration.	Neutral

6.1 By ensuring that there are no negative margins on tariff components for LDNOs, the first two charging objectives are better met as it reduces the potential for adverse impact on competition in the distribution of electricity which results from artificial negative margins.

6.2 The third charging objective is also better met as there is no economic justification for a negative margin to be more cost reflective in these scenarios and the LDNOs should be entitled to recover, as a bare minimum, the costs incurred in paying DUoS charges associated with the upstream distribution business.

7 Impacts & Other Considerations

7.1 No cross code impact has been identified.

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

7.2 We do not believe that this change proposal has an impact on an ongoing SCR or other significant project. We are aware of the DUoS SCR but note that this change proposal would not be covered by the latest scope of that work as issued by Ofgem. We also note that Ofgem have invited industry to continue to develop quick solutions to existing issues and believe that this falls firmly into that category.

Does this Change Proposal Impact Other Codes?

BSC……………...	☐	MRA………..	☐
CUSC……………	☐	SEC………..	☐
Grid Code……….	☐	REC……….	☐
Distrbution Code..	☐	None……….	☐

Consideration of Wider Industry Impacts

7.3 None.

Confidentiality

7.4 Non-confidential

8 Implementation

Proposed Implementation Date

8.1 1st April 2025.

9 Recommendations