




DCUSA Change Report		At what stage is this document in the process?
<div>DCP 438</div> <div>Rate of Return</div> <div>Date Raised: 27/02/2024</div> <div>Proposer Name: Babatunde Olukotun</div> <div>Company Name: National Grid Electricity Distribution</div> <div>Party Category: DNO</div> <div>Governance: Part 1 Matter</div>	01 – Change Proposal	
	02 – Consultation	
	03 – Change Report	
	04 – Change Declaration	
<div>Purpose of the Change Proposal (“CP”):</div> <div>This CP aims to update the rate of return as the previous legal text is out of date.</div>		
<div></div>	<div>This document is issued in accordance with Clause 11.20 of the DCUSA. Parties are invited to consider the proposed amendment and submit their votes using the voting form (attachment 2) to <a href="mailto:dcusa@electralink.co.uk">dcusa@electralink.co.uk</a> by 11 July 2024.</div> <div>The voting process for the proposed variation and the timetable of the progression of the CP through the DCUSA Change Control Process is set out in this document.</div> <div>If you have any questions about this paper or the DCUSA Change Process, please contact the DCUSA by email to <a href="mailto:dcusa@electralink.co.uk">dcusa@electralink.co.uk</a> or telephone 020 7432 3011.</div>	
<div></div>	<div>Impacted Parties</div> <div>CVA Registrants, Suppliers, DNOs and IDNOs</div>	
<div></div>	<div>Impacted Clauses</div> <div><a href="#">Section 1.A</a> Paragraph 1</div> <div><a href="#">Schedule 16</a> Table 3</div> <div><a href="#">Schedule 17</a> Paragraph 2.16, Paragraph 9.2 and Annex 2</div> <div><a href="#">Schedule 18</a> Paragraph 2.9 and Attachment 1</div>	

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## Timetable

Activity	Date
Initial Assessment Report	20 March 2024
Consultation Issued to Industry Participants	May 2024
Change Report Approved by Panel	19 June 2024
Change Report issued for Voting	20 June 2024
Party Voting Closes	11 July 2024
Change Declaration Issued to Parties	15 July 2024
Change Declaration Issued to Authority	15 July 2024
Proposed Implementation	By no later than the November 2024 DCUSA standard release



Any questions?

### Contact

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## Executive Summary

### What?

- 1.1 This change proposal aims to update the rate of return as the previous legal text is out of date.

### Why?

- 1.2 According to the current industry legal text:

**Annuity rate of return** *Set to equal the latest pre-tax real weighted average cost of capital (CC below) for each DNO Party calculated using the following formula:*

$$CC = (\text{Gearing Assumption} \times \text{Pre-Tax Cost of Debt}) + (1 - \text{Gearing Assumption}) \times (\text{Post Tax Cost of Equity} / (1 - \text{Corporation Tax Rate}))$$

*where:*

*Gearing Assumption is set to the 'notional Gearing' value referred to in the ED1 Price Control Financial Handbook;*

*Pre-Tax Cost of Debt is set to the 'cost of corporate debt' value specified in or calculated in accordance with the most recent Annual Iteration Process applicable when setting distribution Use of System Charges;*

*Post Tax Cost of Equity is set to the 'cost of equity' value referred to in the ED1 Price Control Financial Handbook; and*

*Corporation Tax Rate is the rate of corporation tax which is, when setting distribution Use of System Charges, expected to be applicable in respect of the regulatory year (as defined in the Distribution Licence) in which those Charges will take effect.*

*The CC value is calculated as a percentage, and rounded to two decimal places.*

- 1.3 There is a need to update the above legal text so that it does not refer to ED1 price control period as it is no longer relevant.

### How?

- 1.4 The parts that will need to be changed are the 'Gearing Assumption', the 'Pre-Tax Cost of Debt' and the 'Post-Tax Cost of Equity' as these refer to previous price control period. The suggestion is to remove reference to previous price control period.
- 1.5 The cells in the Price Control Financial Model (PCFM) that these could refer to are:
- Gearing assumption – 'Notional gearing' taken from worksheet "InputSummary" row 180;
  - Pre-tax cost of debt – 'Allowed return on debt' taken from worksheet "InputSummary" row 158;
  - Post-tax cost of equity – 'Allowed return on equity' taken from worksheet "InputSummary" row 173;
  - Corporation tax – 'Corporation tax rate' taken from worksheet "InputSummary" row 264.
- 1.6 We suggest the wording does not refer to the rows, but instead just the names, as the format of the PCFM may change.

## Governance

- 1.7 This CP is classified as a Part 1 matter and will go to the Authority for determination, after the voting process has completed.

## Why Change?

- 1.8 There is a need to update the legal text referred to in paragraph 1.2 above, so that it does not refer to the ED1 price control period as this is no longer relevant.

## Working Group Assessment

- 1.9 The DCUSA Panel established a Working Group to assess this CP. This Working Group consists of DNO representatives. Meetings are held in open session and the minutes and papers of each meeting are available on the DCUSA website – <http://www.dcuda.co.uk>.
- 1.10 The Working Group discussed the need for the CP and unanimously agreed with the principles of the CP.
- 1.11 The Working Group issued a consultation to gather information and feedback from market participants.

## Consultation Responses Review

- 1.12 The consultation was issued on 7 May 2024. There were a total of six responses received.
- 1.13 Set out below are the questions that the Working Group sought views on, and a summary of the responses received. The full set of responses and the Working Group's comments are provided in attachment 3.

### Question 1 - Do you understand the intent of this CP?

- 1.14 The Working Group noted that all respondents understood the intent of the CP.

### Question 2 - Are you supportive of the principles of this CP?

- 1.15 The Working Group noted that all respondents supported the principles of the CP.

### Question 3 - Are you aware of any other areas of the DCUSA that may need to be updated, within the scope of this CP? Please provide your rationale.

- 1.16 The Working Group noted that no respondents identified any other areas of the DCUSA that would need to be updated.

**Question 4 - Does the reference in the proposed legal text to the latest version of the PCFM allow for the transition between price setting journeys from one price control period to the next? Please provide your rationale.**

- 1.17 The majority of respondents agreed that the proposed legal text to the latest version of the PCFM allowed for the transition between price setting journeys from one price control period to the next.
- 1.18 Two respondents stated concerns around whether there would be an updated PCFM for use in December 2026 when setting 2028/29 tariffs, with one respondent suggesting amended legal text to future-proof for this eventuality. The Working Group's assessment of the feedback on the legal text is captured under question 8, later in this document.

**Question 5 - Do you consider that this CP better facilitates the DCUSA Charging Objectives? Please give supporting reasons.**

- 1.19 The Working Group noted that all respondents agreed that this CP better facilitates the DCUSA Charging Objectives, with three of the respondents specifically agreeing with the Working Group's assessment of this.

**Question 6 - Are you aware of any wider industry developments that may impact upon or be impacted by this CP?**

- 1.20 The Working Group noted no respondents identified any wider industry developments as being impacted by this CP.

**Question 7 - Are you supportive of the proposal to implement this CP by no later than the November 2024 DCUSA standard release?**

- 1.21 The Working Group noted that all respondents supported the proposed implementation date.

**Question 8 - Do you have any comments on the draft legal text?**




- 1.22 The Working Group noted the amendments suggested by Northern Powergrid (NPg) and amended the legal text accordingly.
- 1.23 The Working Group noted the two options for amendments suggested by Electricity North West (ENWL):
- option 1 – specify the use of the most recent year and the latest published PCFM; or
  - option 2 – allow the DNO to prepare a forecast of the value to be used in the CC formula instead.
- 1.24 The Working Group agreed that its preferred approach was to allow the DNO to prepare a forecast of the value to be used in the CC formula instead and agreed the legal text accordingly. The Working Group discussed that the proposal lacks some transparency, but that the information could be made available to customers if requested.
- 1.25 The Working Group discussed SSEN's proposed legal text amendments to make it clearer where, in the PCFM, the legal text is referencing. The Working Group agreed to make the proposed amendments to the legal text, noting that any future changes to the PCFM would require housekeeping changes to the DCUSA to update the references accordingly.

## Working Group Conclusions & Final Solution

- 1.26 The Working Group reviewed the responses and noted that:
- all respondents understood the intent of the CP;
  - all respondents supported the principles of the CP;
  - all respondents agreed that this CP better facilitates the DCUSA Charging Objectives; and
  - all respondents supported the proposed implementation date.
- 1.27 The Working Group considered the proposed legal text amendments provided by NPg, ENWL and SSEN, and agreed that:
- the proposed amendments by NPg be made;
  - the proposed amendments by ENWL, in the form of option 2 above, be made; and
  - the proposed amendments by SSEN be made.
- 1.28 The Working Group agreed that the proposed implementation should be by no later than the November 2024 DCUSA standard release.

## Relevant Objectives

- 1.29 For a CP to be approved it must be demonstrated that it better facilitates the DCUSA Objectives. There are five general objectives and six charging objectives. The Working Group agreed that this CP should be assessed against the charging objectives.
- 1.30 The Working Group considers that the following charging objectives are better facilitated by this CP:

	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

<input checked="" type="checkbox"/>	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	Positive
<input type="checkbox"/>	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
<input checked="" type="checkbox"/>	6. That compliance with the Charging Methodologies promotes efficiency in its own implementation and administration.	Positive

1.31 The Working Group agreed, and noted that all consultation respondents agreed, that charging objectives 1, 2, 3, 4 and 6 are better facilitated by this CP as it removes references to the ED1 price control period, which is no longer relevant, and future proofs the legal text.

## Impacts & Other Considerations

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

1.32 The Working Group has not identified any impacts to SCRs or other significant industry change projects.

### Consumer Impacts

1.33 The Working Group has not identified any impacts to consumers.

### Environmental Impacts

1.34 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 such material impact on greenhouse gas emissions arising from the implementation of this CP.

### Engagement with the Authority

1.35 This is a Part 1 Matter and meetings are conducted in open governance. The Authority was invited to, and could, join the Working Group as an observer.

## Implementation

1.36 The proposed implementation date for this CP is by no later than the November 2024 DCUSA standard release (due to be published on 7 November 2024) for use for the charging year 2026/2027.

## Legal Text

1.37 The legal text for this CP is provided as attachment 1.

1.38 The Working Group has considered the legal text and is satisfied that it meets the intent of the solution.

## Code Specific Matters

### Modelling Specification Documents

1.39 Not applicable.

### Reference Documents

1.40 Not applicable.

## Recommendations

1.41 The Panel approved this Change Report on 19 June 2024. The Panel considered that the Working Group has carried out the level of analysis required to enable Parties to understand the impact of the proposed amendment and to vote on this CP.

1.42 The Panel has recommended that this report is issued for voting and DCUSA Parties should consider whether they wish to submit views regarding this CP.

## Attachments

- Attachment 1 – DCP 438 Legal Text
- Attachment 2 – DCP 438 Voting Form
- Attachment 3 – DCP 438 Consultation Responses & Working Group Comments
- Attachment 4 – DCP 438 Change Proposal Form