

Proposed variation:	Distribution Connection and Use of System Agreement (DCUSA) DCP359: Ofgem Targeted Charging Review (TCR) Implementation – Customers: Who Should Pay?		
Decision:	The Authority ¹ directs this modification ² be made ³		
Target audience:	DCUSA Panel, Parties to the DCUSA and other interested parties		
Date of publication:	30 September 2020	Implementation date:	In accordance with Clause 11.9A(2) of DCUSA 30 September 2020

Background

In November 2019, we published our Decision (and associated Direction) on the Targeted Charging Review (TCR) Significant Code Review.⁴ Once the Decision is implemented, the costs of operating, maintaining and upgrading the electricity grid will be spread more fairly and, through reducing harmful distortions, will save consumers approximately £300m per year, with anticipated £4bn-£5bn consumer savings in total over the period to 2040.

The TCR included a review of how residual network charges are set and recovered. The aim of the TCR is to ensure that these charges are recovered from network users in a way that meets the TCR Principles:

- reducing harmful distortions,
- fairness, and
- proportionality and practical considerations.

We decided that residual charges should apply to final demand consumers only and that they will be fixed charges, with implementation of these changes in 2022. For distribution residual charges, we decided that domestic consumers should pay a single residual charge set for each licensed distribution area, and non-domestic consumers should be charged on the basis of a set of fixed charging bands, also set for each licensed distribution area. In our decision, we included provisions to review and revise (as appropriate) these charging bands and their boundaries so that the outcome of such reviews can be implemented alongside the commencement of each new electricity transmission price control. The fixed charging bands will be published at a national level and shall be set for each licensed distribution area.

Alongside our decision, we issued a Direction⁵ to the Distribution Network Operators (DNOs), to bring forward proposals to modify the Distribution Connection and Use of System Agreement (DCUSA) in relation to residual charges, to give effect to the terms of the TCR Direction.

DNOs recover their allowed revenue from their customers through distribution use of system (DUoS) tariffs. Currently, the residual component of DUoS tariffs is added once forward-looking charges have been applied, to recover the remaining allowed revenue for network companies set under the price controls.

¹ References to the "Authority", "Ofgem", "we" and "our" are used interchangeably in this document. The Authority refers to GEMA, the Gas and Electricity Markets Authority. The Office of Gas and Electricity Markets (Ofgem) supports GEMA in its day to day work. This decision is made by or on behalf of GEMA.

² 'Change' and 'modification' are used interchangeably in this document.

³ This document is notice of the reasons for this decision as required by section 49A of the Electricity Act 1989.

⁴ https://www.ofgem.gov.uk/system/files/docs/2019/12/full_decision_doc_updated.pdf

⁵ https://www.ofgem.gov.uk/system/files/docs/2019/11/dcusa_direction_1.pdf

The modification proposal

Four DCUSA modification proposals were raised to implement the distribution residual charging reforms resulting from the TCR Decision. Northern Powergrid (the 'Proposer') raised modification DCP359 (the 'Proposal') on 14 January 2020.⁶ It was progressed as part of a Joint Working Group alongside the equivalent proposed modification to transmission residual charges.⁷

DCP359 aims to identify which customers are liable for a residual fixed charge. In line with the TCR Direction, the Proposal would introduce new defined terms for 'Final Demand' and 'Single Site'. It would introduce an additional defined term to tie the two together, namely 'Final Demand Site', to aid in the development of the legal text.

The Proposal stated that all sites with metered import consumption shall be considered a Final Demand Site, and therefore liable for a fixed residual charge, unless they meet criteria to be classed as a 'Non-Final Demand Site' (intended to capture stand-alone storage and generator sites). Therefore, in addition to the new defined terms above, the Proposal would also introduce the following defined terms:

- 'Non-Final Demand Site';
- 'Electricity Generation'; and
- 'Electricity Storage'.

The Proposal would require a generator or storage facility to provide a valid certificate stating that its facility meets the criteria of a Non-Final Demand Site. It would include a transition period to enable Single Sites to provide valid certification to either:

- confirm that they are a Non-Final Demand Site (where they have already been classed as such); or
- provide the necessary evidence that they should be classed as a Non-Final Demand Site (where they have been classed as a Final Demand Site).

The Proposer believes that the modification would better facilitate two of the DCUSA Charging Objectives:⁸

- The first DCUSA Charging Objective, by ensuring DNOs are compliant with licence requirements in relation to Significant Code Reviews (SCRs), by implementing specific requirements set out in the TCR Decision.
- The second DCUSA Charging Objective, by removing an existing distortion to competition whereby storage-only sites may be exempt from residual charges but other generators may not.

Alongside this decision, we are publishing a decision to approve related modification proposals DCPs 358 and 360, which cover the same new section of legal text in the DCUSA and are due to be implemented at the same time.⁹

⁶ <https://www.dcusa.co.uk/change/ofgem-targeted-charging-review-implementation-customers-who-should-pay/>

⁷ The Connection Use of Systems Code seeks to define these terms consistently in CMP334, <https://www.nationalgrideso.com/industry-information/codes/connection-and-use-system-code-cusc-old/modifications/cmp334>

⁸ The DCUSA Charging Objectives are set out in Standard Licence Condition 22A Part B of the Electricity Distribution Licence.

⁹ DCP358: *Determination of Banding Boundaries* and DCP360: *Allocation to Bands*.

DCUSA Parties' recommendation

In each party category where votes were cast,¹⁰ there was majority (>50%) support for the Proposal. For the majority of party categories where votes were cast there was majority support for its proposed implementation date. In accordance with the weighted vote procedure, the recommendation to the Authority is that DCP359 is accepted. The outcome of the weighted vote is set out in the table below:

DCP359	WEIGHTED VOTING (%)									
	DNO		IDNO ¹¹		SUPPLIER		CVA REGISTRANT		GAS SUPPLIER	
	Accept	Reject	Accept	Reject	Accept	Reject	Accept	Reject	Accept	Reject
CHANGE SOLUTION	100	0	100	0	60	40	None	None	N/A	N/A
IMPLEMENTATION DATE	74	26	100	0	43	57	None	None	N/A	N/A

Our decision

We have considered the issues raised by the Proposal and the Change Declaration and Change Report issued on 17 June 2020. We have also considered and taken into account the responses to the consultation that the Working Group issued and the votes of the DCUSA Parties on the Proposal, which are attached to the Change Declaration. We have concluded that:

- implementation of the Proposal will better facilitate the achievement of the DCUSA Charging Objectives; and
- directing that the modifications be made is consistent with our Principal Objective and statutory duties.¹²

Reasons for our decision

We consider the Proposal will better facilitate the first, second and third Applicable DCUSA Charging Objectives and has a neutral impact on the other relevant objectives.

First Applicable Charging Methodology Objective – that compliance with the Relevant Charging Methodology facilitates the discharge by a Distribution Services Provider¹³ of the obligations imposed on it under the Act and by its licence

The Working Group unanimously agreed with the Proposer that DCP359 would better facilitate the first DCUSA Charging Objective. The majority of DCUSA voting parties also agreed with this view. They highlighted that the Proposal ensures DNOs are compliant with licence requirements in relation to the SCR, by implementing specific requirements set out in the TCR Direction. In particular, the Proposal adopts the definition of Final

¹⁰ There are currently no gas supplier parties.

¹¹ Independent Distribution Network Operator

¹² The Authority's statutory duties are wider than matters that the Parties must take into consideration and are detailed mainly in the Electricity Act 1989 as amended.

¹³ Distribution Services Provider: 'means any Electricity Distributor in whose Electricity Distribution Licence the requirements of Section B of the standard conditions of that licence have effect (whether in whole or in part).'

Demand specified in the TCR Direction and enables charges to be levied on a single site basis, consistent with the TCR Direction.

Two DCUSA voting parties highlighted concerns against this objective. One considered that an alternative definition of a single site, which was considered by the Working Group, but not ultimately chosen, better dealt with complex sites (which were ultimately de-scoped from the Proposal, to be covered instead by an existing modification proposal, described below). The voting party considered the alternative option would have better enabled DNOs to identify and define complex customers, and ensure they are charged fairly. Another voting party considered that a domestic non-final demand category should be included now to avoid a lengthy process in future if this band is required.

Our Position

We agree that DCP359 better facilitates this objective, as the Working Group has brought forward a proposed solution that meets the TCR Direction and the intent of the TCR Decision. In addition to the definitions of Final Demand and Single Site, the Proposal also includes definitions for related terms, such as Non-Final Demand Site, to ensure residual charges can be allocated in line with the TCR Direction.

The Proposal also ensures that the IDNO charging regime will continue to function as it does today, consistent with our TCR Direction. For complex sites and private wires, the Working Group highlighted that there is an existing proposed modification considering the charging arrangements in these circumstances (DCP328).¹⁴ DCP328 is currently on hold and will restart following our decisions on the DCUSA TCR proposed modifications.

We note the potential advantage raised by the voting party of using the alternative Single Site definition. But we agree with the conclusion of the Working Group that DCP328 is an appropriate forum to consider these issues in more depth as that modification would affect both forward-looking and residual charges and would allow consideration of a more appropriate solution for these sites in the round. We consider this to be a proportionate approach to these sites given they are relatively few in number and may require a bespoke approach.

We also note that the alternative Single Site definition had the potential to introduce a definition of 'premises' that is at odds with the definition found in some Bilateral Connection Agreements, which could lead to ambiguity in the terms.

Under DCP359, customers connected to complex sites and private wires that currently receive a residual charge will continue to do so. DCP328 focuses on private networks; if the proposed solution for DCP328 does not apply to complex sites (that are not part of private networks), we would expect a party to propose a modification to address residual charging for such complex sites. For the avoidance of doubt, nothing in this letter in any way fetters our discretion with respect to DCP328.

Under the Proposal, all domestic consumers would be considered final demand. In response to the request of one voting party that a domestic non-final demand category should be included, we have not been presented evidence for why such a category would be appropriate. Should a DCUSA Party consider that such a category is necessary, it can choose to propose a modification that we will assess on its own merits.

¹⁴ DCP 328 'Use of System Charging for Private Networks with Competition in Supply'
<https://www.dcusa.co.uk/change/use-of-system-charging-for-private-networks-with-competition-in-supply/>

Second Applicable Charging Methodology Objective – that compliance with the Relevant Charging Methodology 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 the participation in the operation of an Interconnector

The Working Group unanimously agreed with the Proposer that DCP359 would better facilitate the second DCUSA Charging Objective. The majority of DCUSA voting parties also agreed with this view. They highlighted that the Proposal would exempt generation-only sites from residual charges, consistent with the treatment of storage-only sites, removing a perceived distortion to competition. Other comments considered that the Proposal would ensure network costs are recovered fairly from users.

Some voting parties highlighted potential concerns with the distinction between Final Demand and Non-Final Demand. They considered this to be a binary distinction that could lead to distortions in competition. For example, storage or generation sites with a small amount of onsite final demand, or where there is a separate import-only connection to service auxiliary loads necessary for generation, would be treated as Final Demand. One party also suggested more time should be given to developing a more nuanced solution for the difference between Final Demand and Non-Final Demand. Another party concluded that the disputes process for the designation of sites would be able to adequately address any such issues, without the need for potentially expensive reconfiguration of the metering of such sites.

Our Position

We consider that DCP359 better facilitates this objective. We think that current charging arrangements for the recovery of residual charges are distortive and lead to network costs being disproportionately recovered from certain network users. We consider that residual charges should be paid by final demand consumers to reduce the potential for distortion and improve competition between different types of generators. In particular, we consider that this Proposal better facilitates competition by enabling generation-only sites to be treated on an equivalent basis to storage-only sites for the purposes of residual charging.

We note the concerns raised about the classification between Final Demand and Non-Final Demand. We agree that the binary distinction is a practical means of applying residual charges given the precise definition of Final Demand in our TCR Direction. We consider that the Proposal makes appropriate arrangements for the classification of such sites and the opportunity for sites to challenge any classification as part of the transitional arrangements up to October 2021 (the separate Disputes Process is covered by DCP360).

Third Applicable Charging Methodology Objective – 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

No comments were made with respect to the third DCUSA Charging Objective by the Proposer, Working Group or DCUSA voting parties, all of whom considered DCP359 neutral against this objective.

Our position

We consider DCP359 better facilitates the third DCUSA Charging Objective. As stated in the TCR Decision, we consider that distortions to the effects of cost-reflective signals can be reduced by placing residual charges onto final demand users only. DCP359 gives effect to our decision to apply residual charges to final demand, removing this distortion and therefore improving the cost-reflectivity of charges faced by users.

Implementation of DCP359

The proposed implementation date of DCP359 was 1 August 2020, in advance of charges taking effect from 1 April 2022. This implementation date is aligned with DCPs 358 and 360, which cover the same section of DCUSA legal text.

A number of voting parties commented on the implementation date, with the weighted voting of the supplier parties against the proposed implementation date. The comments focused on the impact of Covid-19 and concerns covered the additional disruption to charges at an uncertain time, and the effects on patterns of consumption to the data being used to calculate the charging bands.

These views relate to the implementation of the TCR Decision in general rather than DCP359 in particular, which seeks to define who should pay distribution residual charges. We consider these implementation issues in more detail in our assessment of DCPs 358 and 360, published alongside this decision.

Another party considered that the definition of a residual charge is still under review (under our Access and forward-looking charges SCR) and implementation should be delayed until that term has been defined.¹⁵ While that SCR could change the scale for recovery of forward-looking charges, which may result in a consequential impact on the value of the residual charge, we do not agree that the definition of a residual charge is still under review.¹⁶

We do note that the original proposed implementation date has passed. One of the reasons for delaying this decision was to allow us the chance to consider the final proposed legal text for the equivalent Connection and Use of System Code (CUSC) modification proposals before making our decision on these modifications. Having considered the final proposed legal text for the equivalent CUSC proposals we are now able to issue our decision on these DCUSA proposals.

We note that one of the options for one of the equivalent CUSC modification would exclude reactive power providers from residual charges. In the event that we were to approve that proposal, it would be open to industry parties to bring forward a further modification proposal to the DCUSA to align the treatment under both codes, if appropriate. Please note that nothing in this decision in any way fetters our discretion with respect to our decision on those CUSC modification proposals.

¹⁵ <https://www.ofgem.gov.uk/electricity/transmission-networks/charging/reform-network-access-and-forward-looking-charges>

¹⁶ We considered potential changes to the size of the residual and undertook sensitivity analysis of this in the impact assessment that supported our TCR Decision.

As the original implementation date has passed, we stipulate the implementation date is 30 September 2020 under DCUSA Clause 11.9A(2). The delay to the implementation date does not affect the planned date for the Proposal to be reflected in distribution charges from 1 April 2022.

Impact Assessment

Section 5A of the Utilities Act 2000 imposes a duty on the Authority (its 'Section 5A duty') to undertake an impact assessment in certain circumstances. In particular, that applies where it appears to the Authority that a proposal is important. A proposal is important for these purposes if its implementation would be likely to, among other things, "have a significant impact on persons engaged in commercial activities connected with the ... generation, transmission, distribution or supply of electricity." Where this applies, the Authority is obliged to carry out an impact assessment.

One voting party considered that there should have been an impact assessment at the Working Group stage. We conducted an impact assessment as part of our TCR Significant Code Review which was taken into consideration in our final Decision. The designation of the residual charge to final demand customers, as achieved by DCP359, is consistent with our TCR Decision. DCP359 will give effect to specific aspects of the Decision, and as such, we consider that the impact assessment conducted for the TCR Decision satisfied our obligations under the Utilities Act, with respect to this modification.

Decision notice

In accordance with standard licence condition 22.14 of the Electricity Distribution Licence, the Authority hereby directs that modification proposal *DCP359: Ofgem Targeted Charging Review (TCR) Implementation – Customers: Who Should Pay?* be made.

Andrew Self

Deputy Director, Electricity Access and Charging – Energy Systems Management & Security

Signed on behalf of the Authority and authorised for that purpose