DCUSA CHANGE REPORT

DCP 161–Excess Capacity Charges

1 PURPOSE

1.1 This document is issued in accordance with Clause 11.20 of the DCUSA, and details DCP 161‘Excess Capacity Charges’. The voting process for the proposed variation and the timetable for the progression of the Change Proposal (CP) through the DCUSA Change Control Process are set out in this document.

1.2 Parties are invited to consider the proposed amendments (Attachment 2) and submit their votes using the Voting form (Attachment 12) to dcusa@electralink.co.uk by **08 September 2014.**

2 BACKGROUND

2.1 DCP 161 was raised by Electricity North West and seeks to improve the cost reflectivity of the excess capacity charge calculation within the CDCM and EDCM by removing customer contributions and adding in any additional costs that should be attributed to this charge. This CP also considers applying the excess capacity charge on a monthly, seasonal or time of day basis.

2.2 The Proposer explains that within the Common Distribution Charging Methodology (CDCM) and EHV Distribution Charging Methodology (EDCM), excess capacity is currently charged at the same rate as that applied to the agreed Maximum Import Capacity (MIC) specified within the connection agreement. In addition to this, when a customer breaches their MIC, they are only charged for the month within which the breach occurs, and the Proposer feels that this is not cost reflective for the following reasons:

- The existing capacity charge is discounted to allow for the amount that customers have paid towards the cost of reinforcing the network at the time of connection. Using the existing capacity charge for excess capacity means that this discount is also applied to the excess capacity charge when no customer contributions have been made.
- The excess capacity charge is applied to the month in which the breach occurs. The existing capacity rate is charged and recovered equally for the full year, so the effective excess capacity rate across a full charging year will be less than the rate paid for the existing capacity (except where the MIC is breached by the same amount in every month of the year).

2.3 It is proposed that changing the CDCM/EDCM to calculate a cost reflective excess capacity charge will align the incentives on customers to manage their capacity with the costs incurred by Distribution Network Operators (DNOs). The Proposer feels that this will remove the incentive upon customers to avoid contracting for the capacity they require and place a stronger incentive on customers to manage their capacity more effectively where they wish to avoid elevated capacity charges and should generally cause a reduction in the need for reinforcement to the benefit of all customers.

3 SUMMARY OF THE DCP 161 CHANGE PROPOSAL

3.1 A summary of the amendments proposed within this change report are contained below:

- The CDCM model will be amended to calculate the exceeded capacity charge in the same way as the capacity charge, but with the customer contributions element set to zero.
- The calculation of the exceeded capacity charge for Extra High Voltage (EHV) customers will **not** be amended under this CP.
- The application of the exceeded capacity charge under the CDCM and EDCM will **not** be amended under this CP and will continue to be applied for the duration of the month in which the breach occurs.

4 WORKING GROUPASSESSMENT OF DCP 161

4.1 The DCP 161 Working Group met on 12 occasions. The Working Group was comprised of DNO, Supplier, other interested Parties, as well as Ofgem representation. It is noted that all DCUSA Parties were invited to attend the Working Group. Meetings are held in open session and the documents of each meeting are available on the DCUSA website – www.dcusa.co.uk.

4.2 The Working Group issued two Requests for Information (RFI) and two consultations. These documents are included as Attachments 3, 4, 5 and 6 respectively.

5 REQUEST FOR INFORMATION – APRIL 2013

5.1 The first RFI was issued in April 2013 by the Working Group. The RFI requested that parties provide data relating to the number of customers who have exceeded their Maximum Import Capacity (MIC) in each regulatory year since April 2010 and the revenue recovered from excess capacity charges in each year. The data was provided for each tariff which has a charge for capacity. The total number of customers, total revenue recovered and the number of invoices issued was also requested for comparison purposes.

5.2 The Working Group also requested information relating to the impact on CDCM excess capacity charges of removing customer contributions. A member of the Working Group compiled this information using data from DNOs' published CDCM models, and DNOs were asked to confirm by email that they were happy with the data for their network areas.

5.3 The RFI documents are included as Attachment 3.

6 CONSULTATION NOVEMBER 2013 – SUMMARY & RESPONSES

Consultation 1: Summary

6.1 The Working Group carried out an initial consultation in November 2013 to give DCUSA Parties an opportunity to provide feedback on four options for how the excess capacity charge should be applied. The options considered were:

- To apply the excess capacity charge on a seasonal basis.
- To apply the excess capacity charge on a time of day basis.
- To apply a scaling factor to the excess capacity charge.
- To apply the excess capacity charge based on the maximum exceeded capacity over the last 12 month period.

6.2 The consultation also asked for feedback on a number of other issues including:

- Whether the calculation of the exceeded capacity charge within the EDCM needs to be amended to improve its cost reflectivity.

- Whether exceeded capacity should be addressed through the customer's connection agreement rather than via a higher exceeded capacity charge.

6.3 Following the responses to the consultation, the Working Group decided that the four options for amending the application of the exceeded capacity charge should not be progressed. This was to avoid complexity for end customers and additional billing costs for Suppliers and DNOs. In addition, under option 4, the Working Group felt that fixing the capacity at the highest level from the previous 12 month period reduced the incentive on customers to stay within their MIC.

6.4 The Working Group also agreed that the calculation of the exceeded capacity charge within the EDCM did not need to be amended as it already excluded customer contributions. The Working Group felt that there was an argument that the capacity charge for EDCM customers' needs to be reviewed to take account of customer contributions but that this should be taken forward as a separate CP.

6.5 The majority of consultation responses agreed that use of system charges was an appropriate way to address the issue of customers exceeding their capacity rather than treating it as a breach of the Connection agreement. The Working Group discussed this issue at length and the majority of the Working Group agreed that the two options were not mutually exclusive and that a DNO should be able levy an exceeded capacity charge in addition to trying to resolve the breach through the Connection agreement.

6.6 A summary of the responses received, and the Working Group's conclusions are set out below:

Consultation 1: Responses

6.7 There were 10 responses received to the consultation from DNOs and Suppliers. The Working Group discussed each response and its comments are summarised alongside the collated Consultation responses in Attachment 4.

<u>Question 1 - Do you agree with the intent of DCP 161?</u>

6.8 The Working Group noted that the majority of the respondents agreed with the intent of DCP 161.

Question 2 -Do you agree with the principles of DCP 161??

6.9 The Working Group noted that the responses were split within the consultation as to whether they were supportive of the principles of the CP. The following table provides a break down by respondent type.

Respondent Type	Are you supportive of the principles of the CP?		
	Yes	**No**	**Total**
DNO	4	1	**5**
Supplier	1	4	**5**
Total	**5**	**5**	**10**

6.10 A Supplier respondent noted that they agree that if there is a proven impact on the DNO network then it is appropriate to incentivise customers to only utilise their agreed capacity. However, they remain to be convinced that the DNOs have made the case that this impact is large or real.

6.11 A different Supplier respondent noted that they believe that it cannot be assumed that the majority of customers who regularly breach their agreed MIC level are prepared to accept excess capacity charges rather than have their load requirements reassessed which could result in reinforcement costs being necessary. Customers may genuinely exceed their MIC without realising or due to a temporary increased load.

6.12 The Working Group explained that it could potentially be better addressed/resolved by speaking to the customer to determine their needs. It was explained by DNO representatives on the Working Group that they do communicate with customers when this happens; however, it is often difficult to contact the customer and it does not always remedy the situation.

Question 3 - Do you think that instead of levying higher exceeded capacity charges, DNOs should enforce the connection terms on customers breaching the MIC/MECs?

6.13 The Working Group noted that there was again a split of opinion from the respondents regarding this question. However, the majority of respondents agreed that that it was appropriate to manage customers exceeding their capacity via a higher exceeded capacity charge.

6.14 A DNO Party Respondent explained that they consider that enforcing connection terms is complementary to this proposal rather than an alternative. DNOs currently monitor their customers' MIC/MECs and liaise with a customer when it is breached. This does not remove the need for a cost reflective excess capacity charge which will encourage customers to speak to their DNO and put in place a realistic MIC/MEC. Consequently, this CP will complement the existing contractual arrangement with customers and assist DNOs in managing their connection terms.

6.15 A Supplier Respondent explained that a higher charge may be appropriate if it can be demonstrated that it is reflective of the costs incurred by the network.

6.16 The response goes on to say that the consultation highlights two areas that this DCP is also trying to solve as follows:

- "3.6 A further issue identified by the Working Group is the application of the excess capacity charge. This charge is applied for the month in which the breach occurs. This means that there is a potential gaming opportunity for customers to set their MIC/MEC at an artificially low level and only pay for the additional capacity they require in the months they require it."

- "3.7 DNOs use the MIC/MECs to assist in managing the capacity of their networks. If these are set artificially low, it could lead to DNOs underestimating the capacity required on their networks and not having sufficient capacity to meet the peak network requirements."

6.17 The Respondent also explained that there is a counter argument that a customer may set their MIC/MEC at an artificially high level to prevent competition connecting on the network and leading to artificially high estimation of required capacity on their network which could lead to unnecessary re-enforcement works. Unfortunately this view is not reflected in the consultation. It is hard to see how an excess charge can satisfactorily address either of these issues. They can only be addressed by either enforcing the obligations in their connection agreement or agreeing a variation to that agreement.

Relevant and up to date connection agreements that are enforced are the only sure way to run an efficient network. Simply charging more is not guaranteed to have the desired effect and may lead to unnecessary re-enforcement. The Working Group needs to demonstrate that either of the scenarios exists, and that they truly are causing issues on their networks.

6.18 The Working Group discussed the issues raised within the response and noted that a customer could set capacity artificially high in order to stifle competition in the area. The Working Group felt that this type of issue would be the exception rather than a common occurrence.

6.19 A Working Group member noted that under this CP, there is no incentive to have a higher MIC/MEC, and therefore it is not applicable to the CP.

6.20 The Working Group felt that there is still work to be completed in regard to the efficient management of the network and how to manage capacities better in the future.

6.21 A further DNO Respondent explained that they believe DNOs should look to enforce the connection terms where the customer has breached their agreed MIC/MEC, however this should be done in conjunction with the application of a higher exceeded capacity charge, which will encourage customers to manage their agreed capacity with the DNO.

6.22 A further Supplier Respondent explained that in addition to applying higher exceeded capacity charges, the DNOs can still enforce Connection Terms on these Customers breaching their MIC/MEC. The Working Group reviewed and noted the comments.

Question 4 - Do you believe that any changes to the calculation of excess capacity charges should be made to both the MIC and MEC or just the MIC? Please provide comments.

6.23 A Supplier Respondent believed there may be potential difficulties including export capacity due to the volatility around export sites in terms of capacity particularly reactive elements. It may be a disincentive to export if an excess charge was included against MEC.

6.24 Another Supplier Party explained that in their view it should only apply to the MIC, as exceeding on the MEC does not have the same connotations on the network.

6.25 A DNO Respondent highlighted that within the CDCM, generation does not incur an export capacity charge and therefore this proposal should not impact on those customers in relation to their MEC.

6.26 Another DNO felt that no change to the MIC or MEC should be made.

6.27 The Working Group reviewed the responses and agreed that as generation does not incur an export capacity charge within the CDCM, this is only an issue for the EDCM. As the EDCM was subsequently excluded from this CP, the issue of applying an exceeded capacity charge to the MEC was not considered further.

Question 5 - If DCP 161 is approved and implemented do you anticipate a substantial increase of queries relating to excess capacity charges for DNOs or Suppliers? If so, please provide supporting comments and estimates of the potential impact.

6.28 The Working Group noted that the majority view is that there will be an increase in queries from customers if this CP was implemented; this was the view of DNOs and Suppliers.

6.29 The Working Group noted that the responses were split for this question, with many of the Suppliers feeling that there will be an increase, whilst the DNOs feel it to be a more manageable process.

6.30 A Supplier Party Respondent explained that the impact would in part depend on the roll out of the new changes. Checks would need to take place to ensure the accuracy of the existing MIC in the first instance and communication would need to take place with all impacted customers. Customers may require load management advice to assist with avoidance of costly excess charges and the Supplier anticipated an increase in queries where agreement had not been reached prior to the introduction of this change.

6.31 A DNO Party Respondent explained that they would expect customers (or their consultants) to raise more queries if DCP 161 is approved. The DNO observed that some customers contact their Supplier regarding capacity queries and are then advised to contact the DNO as the MIC/MEC is seen as a DNO charge. The DNO concluded that it would be difficult to quantify the increase in queries.

6.32 Customers would need to be advised in advance of this excess MIC/MEC rate being introduced to reduce the level of queries and give them the opportunity to review and agree changes to their MIC with the DNO. Suppliers are best placed to advise their individual customers.

6.33 Another Supplier Respondent felt that experience has shown that changes to ‘Use of System’ charges does lead to an increase in queries, the majority of which are directed to the Supplier, who is recovering the charges through their supply charges.

6.34 A DNO Respondent noted that they do not believe there will be a substantial increase in the number of queries.

6.35 The Working Group noted the concern from some respondents about who is responsible for the MIC value for each customer and how it is made available to customers. The Working Group highlighted that the MIC is an agreed value between the customer and the DNO and that the DNO is responsible under the National Terms of Connection (paragraph 12.3 of Schedule 2B of DCUSA) for informing the customer of the MIC where the customer does not know the value. The use of system charging statement for each DNO informs customers who to contact regarding their MIC value and this document is available on each DNO’s website.

<u>Question 6 - If DCP 161 is approved and implemented do you feel that there may be more volatility in revenue recovered from excess capacity charges? If so, please give details.</u>

6.36 The Working Group noted that generally, the responses think it will increase, but not significantly.

6.37 A DNO Respondent (ENWL) noted that given the size of their excess capacity charge revenue (£1.4m in 2012/13 out of a total allowed revenue of £439m); they do not expect this to be a material source of volatility. In addition the price signal provided by the more cost reflective excess capacity charge should encourage customers to shift load within their existing capacity limits rather than breach them or to seek an alternative MIC value to reduce the impact of the higher excess capacity charge, so they would expect the number of breaches to decrease under this CP.

6.38 The ENWL Working Group representative explained that they expect volatility to go up, but the materiality will not be significant. However, this should reduce in time once the charge is in place and customers look for ways to avoid it.

6.39 A Supplier Party Respondent explained that in their view there is potential for this volatility especially considering the indicative values that DNO's provided concerning excess rates. The Supplier would like the Working Group to consider how this volatility could be mitigated to ensure other consumers are not impacted by this change.

6.40 The Working Group noted the comments contained within the response and agreed that this will be reviewed during the course of the Working Group.

6.41 Another Supplier Party Respondent explained that in their view this potential additional cost to the Customer may incentivise them to manage their load requirements more effectively, and either keep within their agreed MIC / MEC, or renegotiate a more appropriate capacity.

6.42 A further DNO Party Respondent explained that they do not believe that there will be noticeably more volatility in revenue recovered from excess capacity charges. Total capacity charges only represent a small part of the overall revenue collected and are generally seen as a 'fixed' charge component.

Question 7 - Do you feel that removing customer contributions from the excess capacity charge within the CDCM will lead to this being a more cost reflective element of the charge?

6.43 The Working Group reviewed and discussed all the comments contained within the responses to this question.

6.44 A Supplier Party explained that there may be some merit in this although there needs to be some evidence that all customers have paid a contribution before it is removed.

6.45 A different Supplier Party highlighted that the proposal sounds sensible, but all changes to an econometric model involve a degree of subjective judgement. They feel that the reasons given for the change don't justify the impact on customer billing and supplier/customer goodwill.

6.46 A DNO Party noted that in their view it would marginally, but this is overly complicated compared to the benefit.

6.47 Another DNO Party explained that in their view they believe that removing customer contributions from this part of the charge is appropriate as the customer contributes to their declared capacity at the point of connection. This does create an issue should the customer previously have had a higher declared capacity (which they would have contributed towards) and has since reduced their capacity, which could result in these customers paying twice. However, the opposite would also apply where a customer has increased their capacity since connecting. However, overall they believe that removing customer contributions from the exceeded capacity charge would make this element of the charge more cost reflective.

Question 8 - Do you feel that including customer contributions within the EDCM capacity charge should be considered as part of DCP 161? Please provide supporting comments.

6.48 A DNO Party explained that in their view, no, they believe that an amendment to the EDCM capacity charge (i.e. not just the excess capacity charge) is beyond the scope of this CP as it is a more fundamental change that would affect all customers rather than just those that exceed their capacity.

6.49 A Supplier Party Respondent noted that they believe that a separate change should be raised to fully explore the implications of changes to the EDCM in more detail. We would also encourage that the MIG work on EDCM customer charging is taken into account at this stage also.

6.50 The majority of respondents did not think that the exceeded capacity charge within the EDCM should be included in this CP. The Working Group agreed that the calculation of the exceeded capacity charge within the EDCM did not need to be amended as it already excluded customer contributions. The Working Group felt that there was an argument that the capacity charge for EDCM customers' needs to be reviewed to take account of customer contributions but that this should be taken forward as a separate CP. Consequently, the Working Group agreed not to include the EDCM element within this CP, and to write to the DCUSA Panel to amend the intent, and explain the intention to raise a MIG issue to address the EDCM elements.

Question 9 - There are different options of how this charge can be calculated and applied as explained within paragraph 3.8 of the consultation. Please provide comments on all the options listed, and your preferred option.

6.51 A Supplier Party Respondent explained that all options represent a large change from the status quo, and we don't understand why the simple option of removing customer contributions from the excess capacity rate, and then charging for the month of the breach has not been considered.

6.52 Another Supplier Party highlighted that in their view, none of the options were preferred. It was explained that they see no evidence to move from the current practice of charging just for the month exceeded. We understand that one DNO provided evidence of the level of exceeded capacity when they applied an excess charge greater than the agreed charge. This data was inconclusive as the effectiveness in changing customer behaviour. Unfortunately the Working Group has not presented this data as part of the consultation. They believe this change should demonstrate that charging excess over an extended period is effective in changing behaviour as to the alternatives of amending the connection agreement or charging only for the month of breach.

6.53 A further Supplier Party respondent explained that Option 3 would be their preferred option if they are right in our understanding that this is in essence the same way of charging as at the moment, but just an increase to the published rate from the DNOs and would apply to all customers under that DNO until the next published Condition 4 statements.

6.54 A simple application of an excess rate to any capacity over and above that agreed in the connection terms also seems a simpler and more effective way of charging.

6.55 It was noted by a Supplier Working Group representative that simple application of an excess rate to any capacity over and above that agreed in the connection terms also seems a simpler and more effective way of charging; and the customer can immediately see the financial incentive not to breach the capacity.

6.56 A further Supplier Party Respondent explained the rationale behind each option, setting them out as follows:

- Option 1 – No load management incentive exists for April – October but seems a fairer option for customers who only occasionally breach their MIC assuming the charge is only applied in the month the breach takes place.

- Option 2 – To complex, difficult to explain to customers and reflect on customer invoices. Against the principles OFGEM seem to be promoting around clarity and simplicity.

- Option 3 - Previous year figures may not be relevant following a change of tenancy. Complicated to validate assuming Suppliers had sight of the data used.

- Option 4 - A previous method pre CDCM, leads to complexity with part year supplied sites and Change of Tenancy situations. It is difficult to explain to customers and to replicate on invoices. Customer can be penalised for the whole year even when only breaching the MIC in one month.

6.57 A DNO Party Respondent also explained the rationale behind each option and selecting their preferred option as follows:

- Option 1 – to apply the scaled excess capacity charge on a seasonal basis. This is a sensible option, to protect the network when it is at greatest risk. However, this option does not encourage those customers who exceed all year round to better manage their demand.

- Option 2 – to apply the excess capacity charge on a time of day basis. This option is more protective of the network than Option 1, since it covers every day in the year. Customers will be encouraged to manage their demand all year round.

- Option 3 – to apply a scaling factor to the excess capacity charge. This option is too complex, not as cost reflective and potentially more volatile year on year.

- Option 4 - to apply the excess capacity charge based on the maximum exceeded capacity over the last 12 month period. We do not consider this option the fairest or most cost reflective. Also, a customer who had to pay exceeded capacity charges for an entire year has no incentive to bring their demand in line with

MIC/MEC until the following year.

6.58 It was then explained by the DNO that their preferred option is Option 2.

6.59 Another DNO Party Respondent explained that for their preference: Option 4, followed by option 3. They consider options 1 and 2 to be too complex and would not provide a transparent pricing signal to customers. The Respondent goes on to explain the rationale for each option.

6.60 Option 1: The excess capacity charge will be more cost reflective than under current arrangements, but there will still be a degree of averaging when deriving the charge which will benefit some customers at the expense of others. The charge will not be as transparent as it will apply on a seasonal basis which could confuse customers. This option will require a billing change for Electricity North West.

6.61 Option 2: The excess capacity charge will be more cost reflective than under current arrangements, but there will still be a degree of averaging when deriving the charge which will benefit some customers at the expense of others. The charge will be less transparent than option 1 as it will apply on a time of day basis and traditionally capacity charges have been charged on a daily basis. This option will require a billing change for Electricity North West.

6.62 Option 3: This is the least cost reflective of the options due to the impact of calculating the excess capacity charge based on the average number of times a DNO's customers exceed their capacity each year. However, it is still an improvement on the current situation and this is the easiest to implement as it will not require any billing changes. It will also be the most transparent price signal for customers.

6.63 Option 4: A number of DNOs previously charged for excess capacity using option 4. The price signal is cost reflective and would remove any incentive customers currently have to reduce their MIC below the level they actually require. This will require some billing changes, but the price signal is clear and transparent to customers and this is our favoured option.

6.64 In regard to Option 4, it was queried by Working Group members why it would be considered fair to charge the higher capacity for a year, if the customer only breaches their capacity once. The question was around if it were a one-off occurrence, as compared to a pattern of behaviour, the consequences could be construed as unfair.

6.65 It was noted that the 12 months was historically used, and the principle that they are paying for a capacity charge needs to be the same as the excess capacity charge. It was explained that there is the situation where it is cheaper for a customer to breach capacity, rather than agree a higher level.

6.66 It was highlighted by the Ofgem representative, that the charge needs to be demonstrated to be cost reflective and this may not be the case under option 4 where the customer will incur a higher exceeded capacity charge for 12 months following a breach.

6.67 A further DNO Party Respondent felt that in their view they believe that the exceeded capacity charge should apply at all times when that customer exceeds their declared capacity, they do not believe that seasonal or time of day is appropriate for capacity charging. Option 3 where a scaling factor is used would make this area of the charge more complex for a customer to understand and should not be progressed any further.

Question 10 - If this DCP 161 is approved it is believed that customers (who are charged a tariff containing a capacity element) will need to be informed of the impact. Is this feasible and how would you envisage this communication taking place?

6.68 The Working Group noted that there was a split of opinions given with the responses. The Working Group was also split in the opinions of who should lead the communication efforts to customers. The DNOs felt that the Suppliers have the most up to date contact information and as such would be best placed to lead the communication. The Supplier representatives feel that the DNOs should make the (initial) efforts to communicate with their customers regarding the introduction of these charges.

Question 11 - Do you believe there is a material impact for networks from customers currently exceeding their MIC/MEC? Please provide supporting comments.

6.69 A DNO Party Respondent explained that No, they do not currently experience any material impact from customers exceeding their capacities.

6.70 Another DNO Party Respondent noted that although a customer exceeding their capacity on a single occasion is unlikely to cause an issue for network operators, where this is repeated over a prolonged period of time by a number of parties in a region, the DNO will need to consider reinforcement.

6.71 A Supplier Party Respondent noted that in their view this should be for DNOs to answer, but they have seen no evidence of a material impact on Networks from a MIC/MEC breach.

6.72 The Working Group agreed that more work will need to be completed in regard to demonstrating the impacts for this CP. It was discussed about finding the reinforcement that has been completed that can be attributed to exceeded capacity. Some Working Group members felt that if the 'proof' is not available to demonstrate the issue, it is possible that the justification for this CP could be challenged.

6.73 It was countered that it could also be viewed from a cost reflectivity point of view, and that this CP could influence behaviour in a positive way and lead to more appropriate and cost reflective charges being incurred.

6.74 It was also discussed that there are many ways to manage capacity, and there are customers engaging and doing this with the DNO. However, if a customer isn't doing this and breaching their capacity, it seems fair to charge an excess charge. It was noted that this has logical reasoning, but it needs to be able to be demonstrated.

Question 12 - Are there any unintended consequences of applying these changes?

6.75 The Working Group noted that the majority of respondents did not foresee any unintended consequences.

Question 13 - Do you agree with the implementation date for DCP 161 of 1 April 2015? If not, please provide supporting comments.

6.76 The Working Group noted this would be an area that would be kept under consideration going forward throughout the progression of the CP as there was not a majority view on the implementation date.

Question 14 - Are there any alternative solutions or matters that should be considered by the Working Group?

6.77 A Supplier Party Respondent noted in their view a simple solution of removing customer contributions from the excess capacity rate, and then charging for the month of the breach (as currently done).

6.78 Another Supplier Party Respondent explained that exemptions may need to be permitted to those customers awaiting upgrades, currently in dispute in relation to their connection agreement or change of tenancy situations.

6.79 A DNO Party Respondent explained that they feel that the Working Group should consider how capacity and the application of exceeded capacity should be treated where a single site has two or more MPANs but which are registered to different Suppliers. As an example if a single site has a declared capacity of 500kVA (for the site) and is registered to Supplier A for both MPANs, and they use 400kVA then that Supplier will be charged 500kVA for the capacity charge and nothing for exceeded capacity (as there isn't any). However, if one of those MPANs moves to Supplier B, then the capacity charge could be split between the two MPANs, if so should it be an even split with 250kVA being assigned to each? However for this example if it was split as 250kVA to each MPAN, and then one MPAN or account uses 300kVA, but the other is only using 100kVA then the Customer will see a total of 500kVA for the capacity charge (250kVA for each MPAN/account), and a 50kVA exceeded capacity charge for one of the MPANs. Is this the correct approach? It would be useful to define how this would work within DCUSA as part of this CP.

6.80 The Working Group discussed this point, and acknowledged there is an issue potentially. However, the Working Group highlighted that this will be existing issue with the current methodology and that DNOs should continue to use the current approach but with the new charges if this CP is approved. It was highlighted that this is only likely to impact a very small number of customers.

Question 15 - Are you aware of any wider industry developments that may impact upon or be impacted by this CP? If so, please provide supporting comments.

6.81 The Working Group noted the majority of respondents were not aware of any other industry developments. The other comments were reviewed and discussed by the Working

Group.

7 REQUEST FOR INFORMATION – DECEMBER 2013

7.1 The Working Group issued a second RFI in December 2013. The second RFI requested from DNOs the total agreed capacity, known as 'Maximum Import Capacity' (MIC), and the Sum of the Chargeable Capacity (which equals the MIC and MD); this also showed as a result the total Exceeded Capacity. This illustrated the size of the issue and as a result helped the Working Group to understand the impact of DCP161.

8 CONSULTATION JUNE 2014 – SUMMARY & RESPONSES

Consultation 2: Summary

8.1 The Working Group carried out a second consultation in June 2014 to give DCUSA Parties an opportunity to provide feedback on the proposed solution for DCP 161. The consultation requested feedback on the following:

- The proposal to amend the exceeded capacity charge for CDCM customers by removing the customer contribution element;
- The CDCM model that will be used to implement the CP;
- The legal text required to implement th eCP;
- How the CP could be communicated to customers;
- Any costs associated with the proposed solution.

8.2 A summary of the responses received, and the Working Group's conclusions are set out below:

Consultation 2: Responses

8.3 There were 13 responses received to the consultation from DNO, IDNO and Supplier Parties. The Working Group discussed each response and its comments are summarised alongside the collated Consultation responses in Attachment 5.

<u>Question 1 - Do you agree that the proposed option supports and meets the intent of DCP 161?</u>

8.4 A Supplier Party Respondent explained that they are not convinced that this is the best way to deal with customers who exceed their capacity on the network. This should be dealt with as housekeeping by the DNOs rather than imposing a penal charge. There is currently no evidence provided that supports the case that these customers are causing additional costs on the network.

8.5 The Working Group members present at the meeting were divided in opinion – half who felt that this was not a penal charge, and those who did think so. The members who did not believe this to be the case felt this way because the capacity charge is discounted for customer contributions, but no customer contributions have been made toward the exceeded capacity.

8.6 However, there were members of the Working Group that felt that there was no evidence that the breach was causing the costs and therefore in their view, it is a penal cost levied to customers.

8.7 An IDNO Party Respondent noted that in their view, the proposed solution did not fully meet the intent of DCP 161 as the Working Group have decided not to progress amendments to the EDCM. The IDNO believes the consultation should have set out the Working Group's full reasoning rather than just saying it was because of consultation responses.

8.8 The Working Group did fully consider including the EDCM within this CP, and it was included in a previous consultation. The decision was taken that this was out of scope of DCP 161 and a subsequent CP would be raised in due course following the conclusion of DCP 161.

8.9 The IDNO Respondent went on to say with respect to the CDCM whilst they think the proposal is marginally better than the status quo, there is more that could done to improve the cost reflectivity. Assets are provided for 12 months of the year. Therefore applying a marginal higher charge for excess capacity for one month does not appear to fully address the issue identified. Customers still appear to be incentivised to ask for a lower capacity and take the hit of an additional one month's capacity charges to:

a) Reduce charges in other months when a lower capacity is paid, and

b) To reduce notional connection charges.

8.10 The Working Group highlighted that this was consulted upon as well, and there were concerns that the impact would be too large particularly for customers who only occasionally breach their MIC. Further, there would be no incentive on customers who breach their MIC to reduce their maximum demand below the exceeded MIC level for a further 12 months or the next review period.

8.11 A DNO Party Respondent explained that yes, they agree that the proposed solution improves the cost reflectivity of the excess capacity charge by removing the discount factored into the agreed capacity charge from the customer contributions. They also believe that the proposed solution improves the cost reflectivity of the charge.

Question 2 - Do you have any comments on the proposed CDCM model?

8.12 The Working Group noted that the majority of the respondents had no comments on the CDCM model issued with the consultation.

8.13 A Supplier Party commented that they had no comments on the model. However, they identified some anomalies with the tariffs provided in the impact assessment and the revenue assessment (which suggests that revenue recovered from HH sites is reducing when the excess capacity charges are presumably increasing).

8.14 The Working Group agreed for the Secretariat to contact the parties to give them the opportunity to address the issues before the Change Report is issued.

8.15 The Working Group also discussed the way in which the model allocates indirect/direct and network rates and agreed to address the model so that it is uses the agreed and exceeded capacity rather than just agreed capacity; it was also agreed that the DCUSA modelling consultant would provide an updated Annual Review Pack to accompany the Change Report.

Question 3 - Do you have any comments on the proposed legal drafting?

8.16 The Working Group noted that the overall majority of respondents had no further comments on the legal drafting. It was highlighted by two respondents some formatting issues and some other small items which will be amended prior to the legal text being issued to the DCUSA legal advisors.

Question 4 - Do you have any comments on how this change proposal, if accepted, should be communicated to customers?

8.17 The Working Group noted that the responses to this question were split along Party lines – DNOs v Suppliers. It was also highlighted that the Working Group cannot mandate that certain Parties have to communicate the implementation of a change, only to progress the CP as it is set out. However, it was noted that it was in the best interest of the Industry to communicate effectively. The Working Group also highlighted that a template will be circulated with the Change Report, and subsequently issued to the DCMF MIG for further refinement and progression. The MIG has subsequently agreed to include communication of approved CPs as a standing agenda item.

Question 5 - Do you agree with the implementation date for DCP 161 of 1 April 2015? If not, please provide supporting comments.

8.18 The Working Group noted that the responses to this question were split among the DNO/IDNO and Supplier Parties. The Supplier Parties would prefer an implementation date of April 2016 at the earliest, whilst the DNOs/INDOs would prefer an earlier implementation date.

8.19 A Supplier Party Respondent explained that in their view Customers should have enough notice of this change to either update their capacity requirements with the DNO or look at alternative ways of reducing their capacity, 1st April 16 as an implementation date would give customers reasonable notice.

8.20 Another Supplier Party noted that whilst they would elect for the implementation date to be delayed to April 2017, we would like it to be no earlier than April 2016, as we would like to minimise the number of customers that would be affected by mid-contract changes.

8.21 A DNO Party Respondent explained that yes, they support the implementation date of April 2015. This CP will assist DNOs in managing their network and should be implemented as soon as possible.

Question 6 - Do you consider there to be any costs or development charges associated with the implementation of DCP 161?

8.22 The Working Group noted that there would be some system changes and processes for Suppliers, but no material sums have been identified within the responses. It was identified that an exceeded capacity price already exists, but it was noted that some Parties will still need to make changes to their systems/processes.

Question 7 - Are you aware of any wider industry developments that may impact upon or be impacted by this CP? If so, please provide supporting comments.

8.23 A DNO Respondent noted that under the implementation of P272 if approved, there is a potential increased risk to individual customers in profile class 5 to 8 who move to half hourly settlement before having signed a connection agreement for any reason. In this circumstance these customers would be charged for all of their used capacity at the higher excess capacity rate. However, if DNOs are able to manage the increased volume of connection agreements effectively then this should not be an issue.

8.24 The Working Group noted that this is a potential issue, and is also being discussed within the DCP 179 Working Group.

8.25 Another DNO Party highlighted the significant amount of CPs that could be approved and implemented during the same time and the overall effects are unknown on tariffs. The Working Group noted the points that were raised within that response, but highlighted that the Working Group has to progress each CP on its own merit.

9 BENEFITS AND ISSUES ASSOCIATED WITH DCP 161

Benefits of DCP 161

9.1 The Working Group identified the following benefits that may result from this change, if implemented:

- Exceeded capacity charges will be more reflective of costs as they will exclude the contributions that customers pay towards reinforcement for their agreed capacity when they connect to the DNOs network.

- This change will reduce any potential incentive on customers to set their Maximum Import Capacity (MIC) at a lower level than what they actually require and benefit from lower capacity charges.

- Where a customer needs more capacity, this change will encourage the customer to contact the DNO to agree a Maximum Import Capacity (MIC) that will meet their requirements.

- This CP will assist with network planning by providing greater certainty on future load requirements which will benefit new connectees, please see Attachment 7 for an example of this in practice

9.2 A number of Working Group members challenged whether the benefit of this CP would be material enough to make this CP worthwhile. The proposer produced a case study to highlight a situation where a large customer is regularly exceeding their capacity and driving reinforcement at the primary substation. This case study was issued with the second consultation and is included as Attachment 7. One Working Group member did not agree that the case study provided sufficient evidence and justified this by submitting a written paper to the Working Group which is included as Attachment 8.

Communication of DCP161 to customers

9.3 The Working Group recognised that for DNOs to fully benefit from this Change Proposal, it needed to be communicated effectively to customers in a timely manner. The communication of this change was considered outside the scope of the Working Group as the communication of the CP will need to take place once approved by Ofgem and the Working Group will have been disbanded at that time. However, in recognition of the importance of communication for this CP, a Working Group member has developed a template that can be used by DNOs and Suppliers to inform customers. This template has been passed over to the DCMF MIG group which will develop an engagement strategy to ensure applicable customers are informed of the change ahead of its planned implementation date. In addition, the MIG group has agreed to include communication of approved CPs as a standing agenda item.

Interaction of DCP 161 and the connection agreement

9.4 A number of consultation responses put forward the argument that the exceeded capacity charge relates to a charge for breaching the connection agreement and that as the connection agreement is a contract between the DNO and end customer then any breach of this contract should be resolved between the two parties to the contract. This issue was discussed extensively by the Working Group following the first and second consultations and the following observations and conclusions were drawn:

- The current charging methodology within DCUSA applies an exceeded capacity charge which relates to a breach of the MIC in the connection agreement. This principle will not change under this CP.

- A number of DNO Working Group members highlighted that they attempt to contact the customer when a breach of the MIC occurs. However, it was emphasised that it can be difficult to contact the customer, particularly where the connection agreement was signed many years ago. In addition, if the customer continues to exceed their capacity, the DNOs main recourse is to install equipment to de-energise the site when it exceeds their capacity or to follow a legal route to enforce the contract. However, either of these actions have consequences for the customer and DNO and are not often pursued. Some members of the Working Group thought that a reference to unspecified consequences was not a valid reason to disregard the role of enforcement, and that a DNO would be obliged to enforce MICs in some circumstances in order to ensure that it operated an economic and efficient network and did not discriminate between existing and prospective customers (particularly those who might otherwise have to pay inflated connection charges as a result of the failure to enforce existing capacity limits). The Working Group also noted that DNOs have not pursued the legal and contractual options available to them when they have identified customers exceeding their MIC. This led some Working Group members to question the justification for the change if the current arrangements have not been explored fully.

- It was observed that under the current methodology, there is no financial incentive for customers to stop exceeding their capacity or to agree a more appropriate MIC with their DNO. This CP would provide a greater incentive for the customer to contact the DNO and agree a revised MIC.

- The Working Group was split regarding whether the revised exceeded capacity charge under DCP 161 could be considered a penal charge. A Working Group member believed that the existing exceeded capacity charge is also a penal charge as it relates to a breach in a contract between the customer and the DNO and yet is levied on Suppliers. This point was discussed at length by the working group. They believe that although this charge relates to a breach of contract between the DNO and customer, this does not preclude it from being recovered via use of system charges. This principle is also applied to capacity charges as the MIC is set down within the connection agreement, but the charge for the MIC is recovered via use of system charges through the capacity charge.

Additional Cost to DNO of Customer Breaching MIC

9.5 A number of Working Group members expressed concern that a customer exceeding their MIC will not lead to the DNO incurring any additional costs and therefore the customer should not be charged a higher exceeded capacity rate. This was seen by several Working group members as further justification for why the exceeded capacity charge could be considered penal. In their view, the exceeded capacity charge is levied by the DNO for a breach of the connection agreement, and, being based on typical costs of network reinforcement, it is in excess of the losses or costs that have been shown to be likely to be caused to the DNO by customers exceeding their maximum import capacity. One Working Group member also highlighted that the natural extension of this principle is that DNOs shouldn’t apply any charges for exceeded capacity.

9.6 One Working Group member highlighted that the MIC is a reflection of the capability of the local connection, not the demand on the whole DNO network. They provided an example where an individual customer exceeding their capacity may have a detrimental impact locally, but another customer may have no impact because there is massive excess capacity on the local network. The same effect may occur at times of year or times of day.

The Working Group member was concerned that the whole proposal tries to apply a single national approach to a site specific concern.

9.7 The Working Group acknowledges that the CDCM is an average methodology and that there will consequently be customers who either benefit or are disadvantaged by the averaging approach. This issue affects all the tariff components, not just the excess capacity charge.

9.8 The Working Group acknowledges that the DNO may not incur additional costs when a customer exceeds their capacity. However, the principle already established within the CDCM is that capacity has a value and should be paid for by customers. The Working Group noted that DCP 161 is not amending the principle of charging for capacity, but correcting an anomaly to ensure that capacity charges are only discounted for customer contributions where those contributions have been made. The Working Group acknowledged that in some cases where the customer had reduced their MIC, the customer contribution will have been made on a higher capacity value than the new MIC. However, given that the CDCM is an average methodology, the Working Group felt that it was a reasonable assumption that most customers contributions were made on the basis of their existing agreed capacity value.

Quantitative Evidence

9.9 The Working Group was split and regarding whether there was sufficient quantitative evidence to support the view that excess capacity causes a material issue for network operation. A case study was put forward by the proposer which is contained within Attachment 7. A number of Working Group members did not agree that this case study provided sufficient evidence and one Working Group member produced a critique of the case study which is contained within Attachment 8.

9.10 Another working group member made the following observations:

- The data shown is only for one year, which may or may not be representative over a longer period. There is also no indication whether the peak load was for a long duration of a single HH period.

- There are months, such as Jan & Apr where the targeted customer is below the MIC, yet the primary substation has exceeded its capacity. Similarly for Mar where the targeted customer load has increased, but so has the other customer load. So the whole primary exceeding its capacity cannot be wholly attributed to the single customer. In each of the 12 months shown, the targeted customer load is not the sole reason for the primary exceeding its firm capacity. This example illustrates one of the challenges with this DCP as the potential network reinforcement is caused by multiple customers.
- The example is unusual as the customer accounts for over half the capacity of the primary substation, so any increase has an immediate impact. That would not be the case in the vast majority of cases within the scope of the change as they are connected right across the distribution network at all voltage levels

9.11 It was agreed to circulate a set of questions to all Working Group members to identify individual opinions on key issues associated with DCP 161, the collated responses are included as Attachment 11.

10 FINAL CONCLUSIONS ON DCP 161

10.1 The Working Group's conclusion, reflecting Party opinion as presented in the Consultation responses and Supplementary Questions, is that the proposed drafting meets the intent of DCP 161 and therefore should be issued for voting and Party determination.

11 MODELLING

11.1 The Working Group developed new models to implement DCP 161, the only change made to the EDCM model relates to the application of the discount factor to the CDCM tariffs. The Annual Review Pack has also been amended to include exceeded capacity charges. The models and associated documentation is included as Attachment 9.

12 ENGAGEMENT WITH THE AUTHORITY

12.1 Ofgem has been engaged in the progression of DCP 161 as a member of the Working Group.

13 ASSESSMENT AGAINST THE DCUSA OBJECTIVES

13.1 Working Group considers that the following DCUSA Objectives are better facilitated by DCP 161.

General Objective 1 - The development, maintenance and operation by the DNO Parties and IDNO Parties of efficient, co-ordinated, and economical Distribution Networks

13.2 The majority of the Working Group feels that applying a more cost reflective excess capacity charge may incentivise customers to not exceed their contracted capacity. Some of the Working Group felt that this would reduce the need for reinforcement and therefore promote the development, maintenance and operation by the DNO Parties and IDNO Parties of efficient, co-ordinated, and economical Distribution Networks. One Working Group member felt that the logic in this statement was defective because reducing investment in the network by reducing capacity provided by the network was not necessarily more efficient. However, this point was debated extensively within the Working Group and no other members agreed with this view.

General Objective 3 - The efficient discharge by the DNO Parties and IDNO Parties of obligations imposed upon them in their Distribution Licences

13.3 The Working Group feel that General Objective 3 is better facilitated because DNO parties have an obligation to review their methodologies and bring forward changes where appropriate. Some members of the Working Group felt that the logic in this paragraph was defective because no obligations that would be better facilitated by the implementation of

DCP 161 have been identified. This point was debated extensively within the Working Group.

Charging Objective 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

13.4 The Working Group explained that when a customer expects to exceed their Maximum Capacity they should request an increase from the DNO. Under the Connection Charging Methodology, a proportion of the cost of reinforcing the network will be funded through customer contributions; hence the agreed capacity charge is discounted by such contributions. Where customers exceed their capacity they will not have paid customer contributions in respect of the exceeded amount, and hence receive a discount on excess capacity for which they should not qualify. This proposal seeks to remove the subsidy these customers currently receive in order to align the charges applied for excess capacity with the costs expected to be incurred by DNOs. However, some Working Group members did not feel DNOs had provided sufficient evidence that a DNO running an efficient network would invest in additional network capacity to satisfy demand in excess of MIC rather than enforce connection agreements.

Charging Objective 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

13.5 The Working Group note that DNOs are trying to reduce reinforcement costs to the benefit of all customers and operate in an efficient and low carbon manner. Applying a more cost reflective excess capacity charge should incentivise customers to use their existing capacity more effectively to the benefit of all customers. The Working Group also highlighted that the existing arrangements undermine DNO initiatives trying to encourage greater demand side response as there is no incentive for customers to operate within their agreed MIC. Some members of the Working Group considered that it was not a legitimate Objective of the charging methodology to help DNOs reduce reinforcement costs by discouraging customers from using capacity on the network. This point was debated extensively within the Working Group.

14 DCP 161 – PROPOSED LEGAL DRAFTING

14.1 The DCP 161 legal drafting has been reviewed by the DCUSA legal advisors and is provided as Attachment 2.

15 ENVIRONMENTAL IMPACT

15.1 The Working Group was unable to determine any impact positively or negatively. The Working Group determined that the only relevant environmental impact of the change would arise from any possible reduction in reinforcement by Distributors.

16 IMPLEMENTATION

16.1 The proposed implementation date for DCP 161 is 01 April 2016. The majority Working Group view was for an implementation date of 01 April 2016 reflecting the consultation responses.

17 PANEL RECOMMENDATION

17.1 The Panel approved this Change Report at its meeting on 20 August 2014.

17.2 The timetable for the progression of the CP is set out below:

Activity	Target Date
Change Report Approved by DCUSA	20 August 2014

Panel	
Change Report Issued For Voting	22 August 2014
Party Voting Ends	08 September 2014
Change Declaration	10 September 2014
Authority Decision[1]	15 October 2014
Implementation	01 April 2016

18 NEXT STEPS

18.1 Parties are invited to consider the proposed amendments (Attachment 2), together with the RFIs and Consultations documentation and submit their votes using the Voting form (Attachment 12) to dcusa@electralink.co.ukby **08 September 2014**.

18.2 If you have any questions about this paper or the DCUSA Change Process please contact the DCUSA by email to dcusa@electralink.co.uk or telephone 020 7432 3014.

ATTACHMENTS

- Attachment 1 – DCP 161 CP Form
- Attachment 2 – DCP 161 Proposed Legal Text
- Attachment 3 – DCP 161 RFI April 2013
- Attachment 4 – DCP 161 Consultation November 2013
- Attachment 5 – DCP 161 RFI December 2013
- Attachment 6 – DCP 161 Consultation June 2014
- Attachment 7 –Exceeded capacity case study
- Attachment 8 –Critique of exceeded capacity case study
- Attachment 9 – CDCM Model, EDCM Models & Annual Review Pack
- Attachment 10 – Impact Analysis

[1] Indicative decision date based on the 25 Working Day KPI

- Attachment 11 – Collated Responses to DCP 161 Issues
- Attachment 12 – Voting Form