

Proposed modification:	<b>Distribution Connection and Use of System Agreement (DCUSA) DCP189 – Un-expired Capitalised Operation and Maintenance (O&amp;M)</b>		
Decision:	The Authority <sup>1</sup> directs that modification DCP189 be made <sup>2</sup>		
Target audience:	DCUSA Panel, Parties to the DCUSA and other interested parties		
Date of publication:	17 November 2014	Implementation Date:	1 April 2015

## Background to the Modification Proposal

Before the introduction of the extra high voltage (EHV) Distribution Charging Methodology (EDCM), customers were able to elect to pay capitalised operation and maintenance (O&M), when they connected to the network. This was generally related to sole use assets (SUA)<sup>3</sup>. Not all customers chose to pay it.

SP Distribution (SPD) Limited and SP Manweb (SPM) Limited have a number of EDCM customers who had paid upfront capitalised O&M when they connected. We have granted SPD and SPM time limited derogations<sup>4</sup> (the derogations) for charging years 2012/13 and 2013/14 allowing them to exempt these customers from paying the O&M component of the SUA charge. This was to prevent double charging of O&M costs to these customers and improve cost reflectivity. This modification proposes to amend the EDCM to remove the need for further derogations for SPD, SPM and any other distribution network operators (DNOs) with customers in similar circumstances.

## The modification proposal

DCP189 was raised by SP Energy Networks Limited (the proposer) on 12 August 2013. The modification seeks to exempt EDCM customers with un-expired capitalised O&M payments from paying the direct operating cost element of the sole use asset (SUA) charges in their import charges. This will prevent such customers paying extra in charges for costs already paid for and thereby improve cost reflectivity. The modification proposes to amend the EDCM to have a similar effect to the derogations, ie by allowing the DNOs to exempt these customers from paying the O&M component of the SUA charge for the remaining period of unexpired capitalised charges.

The working group recognised that the DNOs might not be able to identify all customers who had already paid capitalised O&M costs. The proposal defines a customer as qualifying for exemption of O&M charges if it satisfied one of two criteria:

- a DNO and/or the customer has written evidence that the customer (or its predecessors) made a capitalised O&M payment in respect of a connection to the DNO Party's network. Such evidence shall include the period over which the O&M payment was capitalised and that it remains unexpired; or

<sup>1</sup> The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably in this document. Ofgem is the Office of the Gas and Electricity Markets. It supports the Gas and Electricity Markets Authority, the regulator of the gas and electricity industries in Great Britain.

<sup>2</sup> This document is notice of the reasons for this decision as required by section 49A of the Electricity Act 1989.

<sup>3</sup> There may be occasions where capitalised O&M was paid towards joint use assets but the Working Group determined that this is out of scope, as the intent of DCP 189 is limited to sole use assets.

<sup>4</sup> <https://www.ofgem.gov.uk/publications-and-updates/derogation-pursuant-paragraph-13b.14-standard-licence-condition-13b-ehv-distribution-charging-methodology-electricity-distribution-licence-sp-manweb-plc> and <https://www.ofgem.gov.uk/publications-and-updates/derogation-extension-pursuant-paragraph-13b.14-standard-licence-condition-13b-ehv-distribution-charging-methodology-electricity-distribution-licences-sp-distribution-limited-and-sp-manweb-plc>

- customers classified as exempt pre-2005 EDCM distributed generation (DG) are assumed to have paid O&M costs capitalised over a period of 25 years from connection.

The consultation responses generally supported this solution.

The working group considered whether or not exemptions should be retrospective and refunds provided to customers that had already paid capitalised O&M. The working group and all of the consultation respondents agreed that DCP 189 should not be applied retrospectively.

The impact analysis carried out by the working group comprised a schedule of EDCM tariffs and revenues with and without the change. The impact of the change is a reduction in charges for a small number of EDCM customers. However, if more customers come forward with evidence of having paid capitalised O&M charges this number could increase. The discount applied to the fixed charge for eligible EDCM customers in respect of capitalised O&M payments would be recovered from all customers. Although a detailed analysis of the impact on common distribution charging methodology (CDCM) customers was not undertaken the working group agreed that the impact on individual CDCM customers would be minimal.

The working group proposed an implementation date of 1 April 2015. Although the working group recognised that this might not provide much time for customers to provide evidence before the calculation of charges for charging year 2015/16, it considered that delaying the implementation date would prevent many more customers from benefiting from the proposal until much later. Customers providing evidence following the finalisation of charges would qualify for exemption in the following charging year.

The DCUSA Change Report states that the proposal better facilitates DCUSA general objective 3.1.3, and charging objective 3.2.3. It states that the exemption of O&M charges on sole use assets for customers that had already paid capitalised O&M charges is more cost reflective.

### DCUSA Parties' recommendation

The Change Declaration for DCP189 indicates that all parties were eligible to vote. There was unanimous support for the proposal from each party category where votes were cast (no votes were cast in the DG and gas supplier categories). In accordance with the weighted vote procedure, the recommendation to us is that the DCP189 change solution and its proposed implementation date are accepted. The outcome of the weighted vote is set out in the table below:

DCP189	Weighted voting (%)									
	DNO		IDNO/ OTSO		Supplier		DG <sup>5</sup>		Gas supplier <sup>6</sup>	
	A	R	A	R	A	R	A	R	A	R
Change solution	100	0	100	0	100	0	n/a	n/a	n/a	n/a
Implementation date	100	0	100	0	100	0	n/a	n/a	n/a	n/a

### Our decision

We have considered the issues raised by the proposal and the Change Declaration dated 13 October 2014. We have considered and taken into account the vote of the DCUSA Parties on the proposal attached to the Change Declaration. We have concluded that:

<sup>5</sup> No votes were cast in this category of Parties

<sup>6</sup> No votes were cast in this category of Parties

- implementation of the change proposal DCP189 will better facilitate the achievement of the DCUSA Charging Objectives<sup>7</sup>; and
- directing that the change is approved is consistent with our principal objective and statutory duties.<sup>8</sup>

### **Reasons for our decision**

We consider this proposal will facilitate DCUSA Charging Objective 3.2.3 better and has a neutral impact on the other charging objectives.

***DCUSA Charging Objective 3.2.3 – that compliance by each DNO Party with the Charging Methodologies results in charges which, so far as is reasonably practicable after taking account of implementation costs, reflect the costs incurred, or reasonably expected to be incurred, by the DNO Party in its Distribution Business***

We agree with the majority of Working Group members and the majority of respondents who consider that DCP189 facilitates DCUSA charging objective 3.2.3 better. We note that one respondent felt there was insufficient evidence that DCP189 met the objectives better and that it could distort competition to the extent that some EDCM customers' charges would be adjusted whereas those for an equivalent customer under the CDCM would not. The Working Group discussed this comment and observed that there was no equivalent to an EDCM customer under the CDCM. The EDCM is site specific whereas the CDCM is averaged and as such customers will be charged differently. We agree with the working group on this point.

We consider that this proposal meets this charging objective better as it results in more cost reflective charges. Were a customer to be charged for O&M costs on SUA, when they have already paid these costs through capitalised O&M charges when they connected, the DNO would be recovering these costs twice. This change has the same effect as the derogations in ensuring customers do not pay extra charges, and will result in charges that better reflect the true costs of the DNO.

We note that the revenue needed to compensate for the discounts will be recovered from all customers, predominantly those on the CDCM, but that the impact on them will be minimal.

### **Decision notice**

In accordance with standard licence condition 22.14 of the Electricity Distribution Licence, the Authority hereby directs that modification proposal DCP189: 'Un-expired Capitalised O&M' be made.

### **Andrew Burgess**

#### **Associate Partner, Transmission and Distribution Policy**

Signed on behalf of the Authority and authorised for that purpose

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<sup>7</sup> The Applicable Charging Methodology Objectives (Charging Objectives) are set out in Standard Licence Condition 22A Part B of the Electricity Distribution Licence and are also set out in Clause 3.2 of the DCUSA.

<sup>8</sup> The Authority's statutory duties are wider than matters that the Panel must take into consideration and are detailed mainly in the Electricity Act 1989 as amended.