SP ENERGY NETWORKS

Network Planning & Regulation

Your ref

Our Ref

Date

4th February 2019

Contact / Extension

Claire Campbell
0141 614 5851

Andrew Self
Targeted Charging Review, Energy Systems Transition
Ofgem
10 South Colonnade
Canary Wharf
London
E14 4PU

Dear Andrew,

TARGETED CHARGING REVIEW: MINDED TO DECISION AND DRAFT IMPACT ASSESSMENT

I am writing on behalf of SP Energy Networks (SPEN), representing the distribution licensees of SP Distribution plc and SP Manweb plc. We welcome the opportunity to respond to the Ofgem consultation, of 28th November 2018, on "Targeted charging review: minded to decision and draft impact assessment".

Please find attached the detailed responses to the consultation questions. I would be happy to discuss any of the responses further.

Yours sincerely,

Walter Watson

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Energy Income Manager

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APPENDIX: RESPONSES TO CONSULTATION QUESTIONS

CHAPTER 4: HOW WE REACHED THE LEADING OPTIONS

Question 1: Do you agree that residual charges should be levied on final demand only?

Without a definition of "final demand" it is difficult to provide a full response.

SPEN believe that the current distribution methodology, which applies residual to demand customers, is a fair approach as any customer who drives costs on the network should pay an appropriate proportion of the residual.

Currently residual charges are not paid by the generation connection, their associated demand connection will however pay residual. We agree that this approach is fair. Storage customers are using the network in the same way and therefore should pay residual charges for their demand connection. How the demand is used should not influence who should pay residual charges, for example storage connections who use demand to charge a battery and then discharge the energy to be used by other demand customers are not using the network differently to other generators therefore should not be treated differently.

Question 2: Do you agree with how we have assessed the impacts of the changes we have considered against the principles? If you disagree with our assessment, please provide evidence for your reasoning.

In general we agree with the assessment against the TCR principles and distribution impacts, however with regard to the Fixed Charge option the impact on EDCM customers is not fully reflected within the consultation.

Including all EDCM customers within one segment will significantly increase the residual charge to those with small demand supplies. For example a windfarm with a low demand but large generation connection currently pays a small demand charge compared to a customer with a large demand only industrial connection. Applying the same level of charge to both introduces a new distortion with the potential to make such generators unviable. If the minded to fixed charge option is implemented, consideration should be given to differentiating between EDCM customers by grouping into appropriate segments.

Implementing the capacity charge option would be more appropriate for customers with agreed supply capacities, this would remove this potential distortion.

Question 3: For each user, residual charges are currently based on the costs of the voltage level of the network to which a user is connected and the higher voltage levels of the network, but not from lower voltage levels below the user's connection. At this stage, we are not proposing changes to this aspect of the current arrangements. Are there other approaches that would better meet our TCR principles reducing harmful distortions, fairness and proportionality and practical considerations?

SPEN agree with this approach and support making no changes to the current arrangements.

Question 4: As explained in paragraphs 4.41, 4.43, 4.46, 4.49, 4.80, we think we should prioritise equality within charging segments and equity across all segments. Do you agree that it is fair for all users in the same segment to pay the same charge, and the manner in which we have set the segments? If not, do you know of another approach with available data which would address this issue? Please provide evidence to support your answer.

We agree that it is fair that CDCM customers within the same tariff group should pay the same charge. However, we believe a different approach would be better suited to EDCM customers as these customers' characteristics can differ considerably (e.g. by voltage) resulting in significantly different impacts on the network. Whilst we recognise that the recovery of residual charges should be borne by all customers and should not be based on use of the network, the charge must be proportionate and take account of the type of customer.

We do not agree that segments should be set by LLFC. LLFCs are set to allocate losses and are not used to set tariffs. Whilst we recognise they can identify customers, the current DUoS Tariff groups remain the most appropriate method to set charging segments. Further amalgamation of these tariff groups may be required, however they are clearly understood by the industry and DNOs have many LLFCs that apply to different tariff groups, therefore setting charges for each LLFC will add complexity and confusion for everyone.

Question 5: Do you agree that similar customers with and without on-site generation should pay the same residual charges? Should both types of users face the same residual charge for their Line Loss Factor Class (LLFC)?

SPEN agree that similar customers with and without on-site generation should pay the same residual charges. Both drive costs on the network and applying different approaches may discriminate against those who can install generation and those who can't.

Currently within SPEN, customers with or without generation will be on different LLFCs although they may still be within the same tariff group. Therefore the tariff group remains the most appropriate mechanism to determine customer segments.

Question 6: Do you know of any reasons why the expected consumer benefits from our leading options might not materialise?

Without deeper insight and detail of the data, variables or assumptions used in Ofgem's modelling it is difficult to assess, with any degree of certainty, the level of benefit that may materialise. Equally it is difficult to assess if customer behaviour and decision making will change as anticipated in order to deliver the desired benefits.

Question 7: Do you agree that our leading options will be more practical to implement than other options?

SPEN agree that the fixed charge and agreed capacity options are the most straight forward to implement within current systems especially if tariff groupings were used for segments rather than LLFC. Using tariff groups remains the most practical and easiest option to implement.

Question 8: Do you agree with the approaches set out for banding (either LLFC or deeming for agreed capacity)? If not please provide evidence as why different approaches to banding would better facilitate the TCR principles.

We agree with the minded to position in relation to a fixed charge for customers without an MIC as determining the MIC for those customers is not possible. It should also be noted that deemed MIC may not reflect a change in a customer's supply characteristics for example, a change in demographic or moving from a traditional gas boiler to low carbon technology, such as a heat pump. However, for other customers with an agreed MIC the capacity is an appropriate basis by which to set residual charges.

Question 9: Do you agree that LLFCs are a sensible way to segment residual charges? If not, are there other existing classifications that should be considered in more detail?

As stated in question 4, we do not agree that segments should be set by LLFC. LLFCs are set to allocate losses and are not used to set tariffs. They can identify customers, however the current

DUoS Tariff groups remain the most appropriate method to set charging segments and are clearly understood by the industry. DNOs have many LLFCs that apply to different tariff groups, therefore setting charges for each LLFC will add complexity and confusion.

CHAPTER 5 – QUANTIFYING THE BENEFITS OF REFORM

Question 10: Do you agree with the conclusions we have drawn from our assessment of the following?

a) distributional modelling
b) the distributional impacts of the options
c) our wider system modelling
d) how we have interpreted the wider system modelling?

Please be specific which assessment you agree/disagree with.

The conclusions within the document are unclear and difficult to fully assess, however, the qualitiative modelling supports the view that reforming the residual charges will have benefits.

We agree with the conclusion drawn from the behaviour analysis appears to be that there will be little impact on a customer's usage patterns, this is consisent with the the impact of other changes, for example the introduction of locational charging within the EDCM.

We recognise the limitations of the analysis undertaken given the incomplete datasets used (e.g. the ommission of EDCM customer information due to confidentiality). In addition, only one DNO area has been used which may not be representive.

CHAPTER 6 – REMAINING EMBEDDED BENEFITS

Question 11: Do you agree with our proposed approach to the reform of the remaining non-locational Embedded Benefits?

N/A.

Question 12: Do you agree with our proposal not to address any other remaining Embedded Benefits at this stage? Which of the embedded benefits do you think should be removed as outlined in xx? Please state your reasoning and provide evidence to support your answer.

N/A.

Question 13: Are there any reasons we have not included that mean that the remaining Embedded Benefits should be maintained?

N/A

CHAPTER 7 – TRANSITIONAL ARRANGEMENTS

Question 14: Do you agree with out proposed approach to transitional arrangements for reforms: a) transmission and distributional residual charges b) non-locational Embedded Benefits? Please provide evidence to indicate why different arrangements would be more appropriate.

For distribution residual charges, SPEN believe an implementation date of April 2022 would best provide a more sufficient notice period to Suppliers and customers, especially given the likely impact on some customers. The previous change to residual charging (DCUSA Change

Proposal 228), which had considerable impacts for certain types of customer was implemented in the year rather than having a phased implementation.

Also, the introduction of the Common Distribution Charging Methodology (CDCM) and the EHV Distribution Charging Methodology (EDCM), were not phased but implemented once the methodology was approved. Having a phased approach introduces complexity and confusion during the transition period. However, the short notice period resulted in a negative reaction and complaints from many customers, which may be avoided if a longer introduction lead time of 2022 was adopted.

CHAPTER 8 – OUR 'MINDED TO' POSITION

Question 15: Do you agree with our minded to decision set out? If not please state your reasoning and provide evidence to support your answer.

With regard to the distribution residual charges, SPEN agree with some aspects of Ofgem's minded to decision.

We believe a mix of applying residual to fixed charges to those without an MIC and capacity charges for sites with a declared MIC is more appropriate than applying the residual to fixed charges for all customer segments.

EDCM customers have customers connected from HVS to 132kV with different characteristics, from demand only customers to wind farms, it is therefore unfair to allocate one fixed charge to all customers in EDCM. We would see significant disturbances for a large majority of our EDCM customers.

In addition, as stated above, we consider using tariff groups to set customer segments is a far better approach than using LLFCs. If DCP 268 (DUoS Charging Using HH Settlement Data) is approved this will reduce the number of tariff groups i.e. LV Network Domestic and Domestic Unrestricted tariffs would be treated as a single segment, this could mitigate the risk of customers moving between the broader segments.

Question 16: For our preferred option do you think there are practical consideration or difficulties that we have not taken account of? Please provide evidence to support your answer.

For distribution residual charges, we do not anticipate any practical difficulties beyond the change to current methodologies and associated models. The process and timeline for this change needs to allow a suitable lead time for customer communication and engagement, especially to those segments that may see significant increases in the levels of their network charge.