



Ofgem  
10 South Colonnade  
Canary Wharf  
London  
E14 4PU

1 June 2021

Dear Sir or Madam

Ref : Ofgem Consultation - Decision on CMP343

Thank you for the opportunity to respond to the Consultation on your minded to decision for CMP343. Please find below E.ON's response.

### Summary

E.ON is pleased to see that Ofgem have revisited some of concerns that have been raised by the industry through the CUSC code modification process of the TCR original decision. We are especially pleased that the question of whether the original TCR decision introduced a new (and unintended) distortion to the market has been fully assessed and considered. This new distortion could allow some customers to consume at the peak and increase the negative contribution that their forward-looking charge made to their overall bill. Whilst this would reduce those customers' bills, it would drive up materially other customers residual charges. We are therefore pleased that the question of whether this is fair (even if it is cost reflective) and how this might be addressed is being tackled.

As you can see from our response below, we are in agreement with Ofgem's current decision to introduce 'flooring at 0' for the forward-looking charge, even though this will lead to some degree of cross subsidisation between customers. We believe that the possibility of an open-ended distortion could introduce much higher inequality costs than the £200m of cross subsidy suggested in the impact assessment. We would have liked to have seen more analysis of how customers might have reacted to this distortion but appreciate that the TCR changes are already running quite late.

With regards to the banding of transmission connected demand for the Transmission Demand Residual (TDR), we also agree with Ofgem that the variability in sizes of transmission connected demand does necessitate more than one band. As the variation in size is broadly similar to those customers who are distribution connected, we agree that they ought to be treated in a similar manner with four bandings at the 40<sup>th</sup>, 70<sup>th</sup> and 85<sup>th</sup> percentiles. However, given the change in

**E. ON UK**  
Westwood Way  
Westwood Business Park  
Coventry  
CV4 8LG  
eonenergy.com

Matthew Cullen  
External Affairs Executive  
matthew.cullen@eonenergy.com

Registered Office:  
Westwood Way  
Westwood Business Park  
Coventry CV4 8LG

residual charge that this would create for the top band (£550k to £2.56m pa) we are also very supportive of Ofgem's consideration to delay the TDR implementation for one year until Apr 2023. Whilst this will mean that DUoS residual and TNUoS residuals will be on different cycles, we believe that very large consuming transmission connected customers need this extra time to make changes to allow for the significantly higher charges expected.

**Q1: Do you agree with our assessment of the distributional impacts of the flooring approaches?**

E.ON is pleased to see that the distributional impacts on all customers are being put front and centre of this consultation. We would have liked to have seen further analysis on customer reaction to the flooring approach as well as a quantification of the cross subsidy between Scotland and England rather than just the static bill impact included in the IA, but we acknowledge the additional delay this would have added to an already late delivery .

As recognised by the working group and Ofgem, the 'no floor' option does present an incentive for some customers to consume during the peak in order to lower their bills by increasing the negative contribution of the forward looking charge to the overall charge thereby creating a new market distortion. Whilst this clearly is against one of the TCR principles (reducing harmful distortions), it is not clear to us the extent to which customers could take advantage of this distortion, its impact on their overall bill and hence the degree of subsidisation between these customers and customers who cannot reduce their bills this way.

We agree that any distortion would be temporary and would hopefully be removed by the Access SCR (due to release its minded to decision later this year). However, we also are conscious that the Access SCR is significantly delayed and has had a complete change in project management recently. Therefore, we are not confident that any temporary distortion would be a short lived one with CMP343 implementation likely to be April 2023, but DUoS reform through the Access SCR likely to be Apr 2024 at the earliest.

We also agree that the TDR should remain a national fixed charge as befits a cost recovery charge and not reintroduce a price signal as would occur under the locational adjustment option. All cost (and hence price) signals should be amalgamated into the forward-looking charge to incentivise the correct market behaviours to support the network.

By flooring the forward-looking charge to zero, customers in Scotland will, in part, be subsidising customers in England which does not strike us as equitable (another one of Ofgem's three principles). According to the IA, this cross subsidy would amount to ~£200m pa but how that amount is distributed between customers is not clear. In order to do this, Ofgem need to consider the behavioural response of Scottish customers to negative forward-looking charges and fixed residual charges. Table 1 considers some high level scenarios of Scottish customers' response to the

distortion and what that might mean in terms of differentials between English and Scottish customers.

Various scenarios of the impact of Scottish customers consuming more at the peak		No flooring			Flooring to zero			Diff
		Forward-looking charge (£ pa)	TDR (£ pa)	Total bill (£ pa)	Forward-looking charge (£ pa)	TDR (£ pa)	Total bill (£ pa)	
1	Scotland	-30	30	0	0	27	27	+27
	England	10	30	40	10	27	37	-3
2	Scotland	-20	30	10	0	27	27	+17
	England	10	30	40	10	27	37	-3
3	Scotland	-10	30	20	0	27	27	+7
	England	10	30	40	10	27	37	-3

Table 1 - Impact of flooring forward-looking charges on Scottish and English customers

However, overall, we agree with Ofgem that the benefit of not introducing another distortion outweighs the cross-subsidisation and equality argument. Therefore, we agree with Ofgem's assessment that a flooring option is the better choice overall.

**Q2: Do you agree that, of the flooring options presented, flooring at 0 best meets the TCR Principles and Applicable CUSC Charging Objectives?**

As stated in Q1, E.ON believes that the trade-off between TCR principles (remove distortions vs. equitable charges) that Ofgem have identified is correct and that the problems of introducing a small amount of cross-subsidisation between Scottish customers and English customers (flooring at 0) are outweighed by the problems caused by a new distortion that incentivises some customers to consume at the peak in order to reduce their overall bill (no flooring). It is not clear to us how large this distortion could be, but it would seem to have the potential to be unconstrained and therefore much larger than the known £200m of cross subsidisation from the flooring to 0 option. For this reason, we would have liked to have seen more analysis on customer reactions to the no flooring option but understand why this has not been possible in the timescales. We are also of the opinion that the introduction of locational adjustments will only set back the overarching principle of the TCR (removing price signals from the residual charge) and therefore does not meet the TCR principle as well as the other two options.

With regard to the Applicable CUSC Charging Objectives (ACO), we agree that the no flooring option adds a distortion which consumers could take advantage of and thereby impact on competition between network users e.g. Scottish manufacturers being able to lower electricity bills simply by consuming at the peak whilst English counterparts would be unable to replicate this cost saving. ACO (a) which refers to

competition is explicit in its consideration of competition between purchasers of electricity.

*“That compliance with the use of system charging methodology facilitates effective competition in the generation and supply of electricity and (so far as is consistent therewith) facilitates competition in the sale, distribution and purchase of electricity”*

Therefore, we agree with Ofgem that the flooring to 0 option is positive against ACO (a) whilst the no flooring option is negative.

However, as stated above, there is a trade-off and the flooring to 0 option clearly is less cost reflective than the no flooring option. ACO (b) is clear that cost reflectivity is a key attribute to any modification. Therefore, we consider the flooring to 0 option negative against ACO (b) and the no flooring option positive.

*“That compliance with the use of system charging methodology results in charges which reflect, as far as is reasonably practicable, the costs (excluding any payments between transmission licensees which are made under and accordance with the STC) incurred by transmission licensees in their transmission businesses and which are compatible with standard licence condition C26 requirements of a connect and manage connection)”*

We believe that neither option helps or hinders ACO (c) (developments in TSO’s business) or ACO (d) (compliance with EU and UK regulation). Also, both options are relatively simple to implement (unlike the locational adjustment option) and therefore are positive against ACO (e) (efficiency).

Therefore, the decision is whether the negatives of introducing a new distortion outweigh the negatives of cross-subsidisation. Given the lack of quantitative evidence on the likelihood for customers to reduce bills, but also that it could potentially be an open ended risk, E.ON agrees with Ofgem that the balance is more in favour of the flooring to 0 option.

**Q3: Do you agree with our assessment of the distributional impacts of the banding approaches?**

We understand that the original banding for transmission connected (T-connected) demand was based on the assumption that the variability in size between T-connected sites was small and that new data has come forward in the intervening period to correct this assumption. From our own portfolio we would agree that T-connected demand spans a large array of consumption and capacity requirements which can differ substantially. Therefore, treating all these customers in the same manner clearly breaks one of the TCR principles of equality/fairness.

The changes to the TDR charge between one band and four bands for the top band is very significant (£675k to £2.57m) and as such we are glad to see Ofgem acknowledge that consumers may have to take measures to adapt to the new

prices. Therefore, we are pleased to see Ofgem recommend a one-year delay into the implementation date to give these customers time to make any necessary changes. But generally, E.ON agrees that increasing the TDR charges for a small sample of very large customers (even by ~£2m pa) is more equitable than charging quite small T-connected customers the same as the very large customers.

**Q4: Do you agree that, of the banding options presented, four bands best meets the TCR Principles and Applicable CUSC Charging Objectives?**

Given the new data about the range in sizes of T-connected demand (over two orders of magnitude), we believe that this brings T-connected demand variability in line with distribution connected demand variability within voltage levels. Therefore, all the arguments that led to distribution connected final demand being split into four bands for each voltage level (i.e. enough bands to capture the variability but a small enough number of bands to ensure sufficient numbers of customers within each band) would also be relevant for T-connected demand.

Regarding the TCR principles, we believe that all the banding options are neutral against removing distortions in the market (as this is tackled by the fixed price per site per day aspect of the TCR). As stated in Q3, we believe that the four-band option is the fairest as it ensures that very small consumers are not treated in the same manner (and charged the same price) as very large consumers, whilst the one band option is the least fair. Whilst increasing the number of T-connected demand bands from one to four introduces a more complex system, we believe that the number of customers this will affect is quite small (<100) and therefore will not create a need for new billing systems across the industry. Therefore, whilst the four-band option is negative against the TCR principle of practicality, it is not excessively impractical.

Against the ACOs, we believe that the creation of a four-band system for T-connected customers is fairer and therefore should in principle improve competition between T-connected consumers. Therefore, we see the four-band option as positive against ACO (a) with the two-band option slightly positive and the one band option neutral. Against cost reflectiveness (ACO (b)), changes to TSO business (ACO (c)) and EU and UK regulations (ACO (d)) we believe that all the options are neutral. Finally, against ACO (e) (efficiency) we believe that although the four-band option adds more complexity, the industry is used to (and has prepared for) multiple bandings at other voltage levels and for larger numbers of customers. Therefore, we do not think that any of the options adds a huge degree of inefficiency to the industry. Overall, we agree with Ofgem that the four-band option offers the best way forward for customers and the industry as a whole.

**Q5: Do you consider that any of the options presented adequately addresses very small users (including those associated with mixed use sites)?**

In terms of the impact that the changes to the banding for T-connected demand will have on very small users with no mixed demand, we believe that Ofgem have presented options that adequately addresses very small users under the 4 band

approach because the variation in charges between percentiles ensures the lowest charges are allocated to very small users which is appropriate as we have outlined in response to Q4. When considering very small users against the 2 band option, we feel that the MWh threshold of 140GWh between 85<sup>th</sup> percentile and all other users is too high and as such would likely have a similar effect that the single banding approach would have for all but the very highest consuming sites by pushing more of the TDR costs onto very small users and less onto medium users. As such we feel that this also goes against one of the TCR principles to ensure that all users pay their fair share of the costs and in turn, only further supports our belief that the 4 band approach ensures a fair and equitable TDR cost allocation is achieved.

In terms of the impact that the changes to the banding for T-connected demand will have on mixed demand users we believe that there is likely to be a wide variation specific to the types of mixed demand user and technologies that could be deployed by the user that will see very small users with mixed use allocated to lower charging band with very small users with no mixed use. We believe that this is fair and consistent as the final demand associated with the different type of users is not a factor provided consumption levels are within the upper tolerance of the 40<sup>th</sup> percentile. Whilst we also perceive a future impact in terms of small or medium users being allocated as very small users because of possible outcomes of CMP 363/4 we agree and are supportive that this is not a consideration as part of the final decision considerations for CMP343.

**Q6: Do you agree with our minded-to decision to approve CMP343 WACM2?**

Overall, we agree with Ofgem's decision to introduce a four-band pricing structure for the TDR for T-connected demand customers as well as flooring the TDR at 0 for all customers. We have based our views on qualitative evidence only and would have preferred to analyse more quantitative data (especially around customer reactions to a 'no flooring' option). We are especially pleased that Ofgem have realised the severity of the changes they are suggesting for very large T-connected customers and fully back the delay to the TCR implementation by one year for T-connected customers.

**Q7: Do you agree with our minded-to decision that implementation should be delayed by a year, until April 2023?**

See response to Q6