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for energy consumers

To interested parties

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Consultation on the inclusion of Access SCR costs in RIIO-ED2

In December 2018, we launched the Access and Forward-Looking Charges Significant Code review (Access SCR)¹, part of a package of reforms relating to how different parties access and pay charges for the electricity networks. The objective of the Access SCR was to ensure that electricity networks are used efficiently and flexibly, reflecting users' needs and allowing consumers to benefit from new technologies and services while avoiding unnecessary costs on energy bills.

In May 2022 we published our final Decision and Direction on the Access SCR², covering two areas of the original scope: the distribution connection charging boundary; and the definition and choice of access rights. As part of our final Access SCR decision, we directed changes to be made to the connection charging arrangements so that customers pay less towards the reinforcement of the existing network that is triggered by their connection. The charging reforms are due to come into effect in April 2023, aligning with the start of the RIIO-ED2 price control.

It is not clear how and to what extent consumers will respond to the changes. However, even in the absence of any further behavioural change, there will be an increase in DNOs' costs as work is funded through the price control that would otherwise have been borne by the connection customer. The Access SCR therefore introduces significant uncertainty in DNOs' forecasting of what investment will be needed in RIIO-ED2.

Our RIIO-ED2 Draft Determinations (DDs)³, published in June 2022, did not reflect the increased costs associated with these decisions, because the final RIIO-ED2 Business Plans submitted by the DNOs in December 2021 could not reflect the final Access SCR decision published in May 2022. We proposed to work with the DNOs following DDs to understand the expected cost impact of these changes to baseline allowances and the design of any appropriate uncertainty mechanisms, and to reflect these in our RIIO-ED2 Final Determinations (FDs) later in 2022. To support this, we invited the DNOs to resubmit their estimated impact of Access SCR related costs on their RIIO-ED2 business plans. These resubmissions were received on 31 August 2022 and further detail is set out below.

¹ [Electricity Network Access and Forward-Looking Charging Review - Significant Code Review launch and wider decision](#)

² [Access and Forward-Looking Charges Significant Code Review: Decision and Direction](#)

³ [RIIO-ED2 Draft Determinations](#)

Ahead of our RIIO-ED2 Final Determinations at the end of this year we are inviting all stakeholders to provide feedback on three proposals. These are:

- Our proposed approach to managing uncertainty around the additional network investment required as result of the Access SCR decision
- Our proposed approach to reflecting the Access SCR decision in baseline allowances
- Our proposed approach to assessing the costs submitted by the DNOs to ensure they are treated consistently.

We set out further detail on each of these areas below.

Managing uncertainty

In our DDs we noted the uncertainty around the impact of the Access SCR on investment requirements for RIIO-ED2, including around how and to what extent users of the energy system will respond to the changes. We recognised that even in the absence of behavioural change, there would be an increase in DNOs' costs as work will need to be funded through the price control that would otherwise have been funded by the connection customer.

In our DDs did not propose a specific uncertainty mechanism (UM) to manage the impact of the Access SCR above baseline allowances. This was because while the DNO will face uncertain costs, whether the driver is the Access SCR or not, is largely irrelevant. What is important is that new network investment is needed. We also noted that there are practical challenges with identifying whether an investment would not have gone ahead in the absence of the Access SCR. We said that our suite of proposed UMs for managing Load Related Expenditure (LRE) uncertainty were an appropriate, and sufficiently robust, means of managing the uncertainty arising from the Access SCR. In their responses to DDs, all DNOs agreed with our approach not to introduce a specific uncertainty mechanism to manage the impact of Access SCR, with some DNOs noting that there would be practical challenges with categorising connections arising as a result of the Access SCR as opposed to those that would have progressed anyway. However, DNOs said that the suite of uncertainty mechanisms proposed at DDs fail to adequately cater for the increase in indirect costs that will be incurred as a result of Access SCR decisions because they do not include indirect cost increases such as network design and engineering costs that may be required to support the additional work due to the Access SCR.

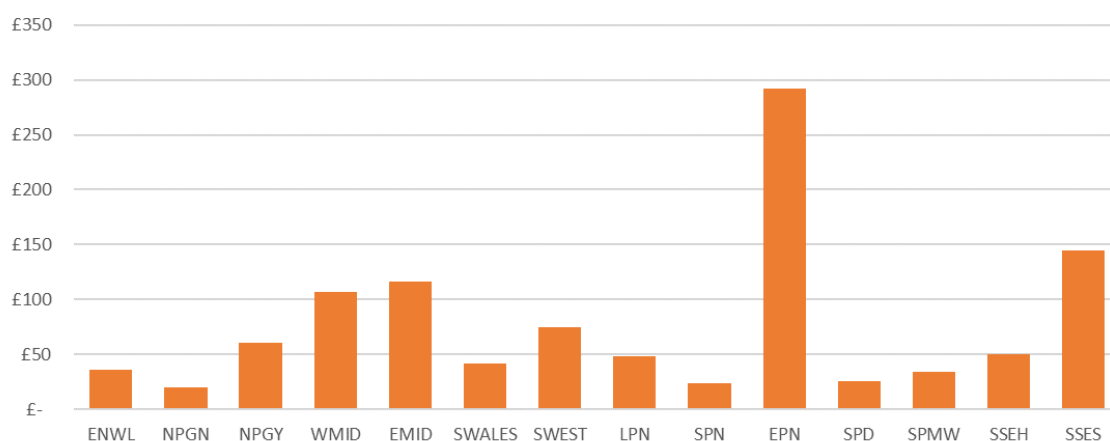
As a result, we are maintaining our proposal not to develop a specific UM to manage the impact of the Access SCR above baseline allowances. Instead we will take forward work to ensure the LRE UM package can manage this uncertainty, including considering whether any changes are required to address indirect costs. We will do this through working groups with the DNOs before confirming our position in our RIIO-ED2 FDs.

Setting Baseline allowances and costs assessment

Access SCR costs were not contained within baseline expenditure for RIIO-ED2 proposed in our DDs. In August 2022 all DNOs submitted ex-ante Access SCR costs, totalling £1.1bn across all DNOs for the five-year period of the RIIO-ED2 control to March 2028.

DNOs have taken different views on what costs can be set ex ante. Northern Powergrid only requested ex ante allowances for the first two years of RIIO-ED2, recognising the challenge of predicting the impact of the Access SCR on customer behaviour above its current understanding of historical customer behaviour. However, other DNOs argue that many impacts of the Access SCR are now more certain and these should be reflected in changes to the ex ante allowances set in our FDs. DNOs have also commented on the challenges of integrating costs within the rest of the LRE allowances.

Submitted RIIO-ED2 Access SCR costs by DNO (£m)



As we did in our DDs, we made pre-modelling adjustments to the DNO submissions to make the costs of the DNOs more comparable with one another and thus produce more robust results. Specifically, we applied adjustments to labour costs to account for regional variations in labour costs. The only inconsistency with our DDs cost assessment approach is that we have not adjusted for company specific factors for LPN, SPMW and SSEH here, whereas we did at DDs because we do not believe the activities overlap. Overall, we have taken a simple approach to the benchmarking of Access SCR costs by applying the overall adjustment made to DNO costs in our DDs and applying that adjustment to their submitted Access SCR costs.

The increase in Access SCR costs is largely driven by the change in customer behaviour as a result of shallower connection charges where costs transition from customer funded to being funded via Distribution Use of System (DUoS) charges. This change impacts several activities that the DNOs carry out, such as connections or primary reinforcement. We have looked at assessing these different cost activities independently. However, we believe this would add unnecessary complexity.

Whilst we acknowledge that there will be additional costs incurred by DNOs as a result of the Access SCR, the DNOs' submissions have not allayed our concerns that two aspects of these costs are very challenging to accurately assess:

- The DNO submissions have not provided us with confidence that they can yet accurately estimate how much more of the connection costs will be paid by DUoS charges.
- We do not consider that any funding should be provided to reflect changes in customer behavior, because this impact has not been robustly quantified.

To reflect this uncertainty we propose to provide ex ante funding for the first two years of RIIO-ED2 of the DNOs' requested Access SCR costs. Where this funding and baseline LRE allowances are insufficient to meet demand, DNOs will be able to seek additional LRE allowances during the LRE Re-opener windows, which following DDs feedback will likely be in January 2025 and January 2027.

Table 1.1. sets out our provisional view of the ex-ante allowances we propose to provide DNOs in our Final Determinations. The costs in table 1.1 are Total Net Costs after Non Price Control Allocation with ED2 Ongoing Efficiency. There is a variance in the submissions from the DNOs with the most notable being EPN. EPNs submission is largely driven by a significant number of Active Network Management schemes moving to firm connections in RIIO-ED2.

Table 1.1: DNO RIIO-ED2 Access SCR allowances

	Access SCR ex-ante allowance (£m, 2020/21 prices)
ENWL	£ 11.6
NPGN	£ 6.6
NPGY	£ 20.2
WMID	£ 34.9
EMID	£ 38.4
SWALES	£ 14.0
SWEST	£ 22.8
LPN	£ 17.5
SPN	£ 8.5
EPN	£ 100.9
SPD	£ 8.9
SPMW	£ 11.7
SSEH	£ 15.3
SSES	£ 45.3
Total	£ 356.7

Questions:

1. Do you agree with our proposals not to have a UM specifically for Access SCR, but instead to manage this uncertainty through the suite of LRE UMs?
2. Do you have any views on how best to manage the potential increase in indirect costs?
3. Do you agree with our proposal to provide two years of ex ante allowances given the uncertainty in this activity?
4. Do you agree with our proposed cost assessment approach and RIIO ED2 ex-ante allowances?

Next steps

This consultation letter allows stakeholders to provide views as to how Access SCR costs should be incorporated in to the RIIO-ED2 Final Determinations. We have set out specific questions regarding the price control framework in this letter. We would welcome written comments on these questions or any other related matters by Friday, 21 October. Please email responses to RIIOED2@Ofgem.gov.uk.

Unless clearly marked as confidential, we will publish responses on our website in due course.

Yours faithfully,

Steven McMahon
Deputy Director, Onshore Networks, Price Control Setting