
Distribution Connection and Use of System Agreement (DCUSA) – DCP450: Managing the effects of surplus residual charge in the CDCM

Decision:	The Authority ¹ directs that this modification be made ²
Target audience:	DCUSA Panel, Parties to the DCUSA and other interested parties
Date of publication:	20 October 2025
Implementation date:	1 April 2027

Background

In November 2024, we published guidance³ to Distribution Network Operators (DNOs) which set out how we expected them to act in the event that the application of the Common Distribution Charging Methodology (CDCM) resulted in excessive surplus residuals for the 2026/27 charging year. A surplus residual can occur when the revenue collected from forward-looking network charges greatly exceeds the revenue required for the operation of the network, requiring forward-looking charge rates to be reduced. The status quo is that in some circumstances, this surplus residual can occur to the extent that built-in adjustment approaches⁴ are exhausted, resulting in a failure to produce a complete set of tariffs.⁵

In particular, our guidance described an alternative approach to the calculation of distribution network charges that could be used to address this defect in the CDCM, conditional upon our approval of a request to derogate from the relevant licence conditions. This alternative approach was to uniformly reduce an input to the charging methodology – the gross asset value of the Distribution Reinforcement Model (DRM or “the 500MW Model”) – which had the effect of reducing the residual surplus to a level such that the existing adjustment process was sufficient to ensure a complete set of tariffs could be produced.

¹ References to the “Authority”, “Ofgem”, “we” and “our” are used interchangeably in this document. The Authority refers to GEMA, the Gas and Electricity Markets Authority. The Office of Gas and Electricity Markets (Ofgem) supports GEMA in its day-to-day work. This decision is made by or on behalf of GEMA.

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

³ The guidance can be reviewed here: [Managing the effects of surplus residual charges guidance | Ofgem](#), which had been informed by stakeholder views at a working level and through our call for input here: [Distribution Use of System Charging – Managing the effects of surplus residual charges | Ofgem](#)

⁴ This adjustment mechanism is described in Paragraphs 94 and 94A of Schedule 16 of the DCUSA.

⁵ We published a detailed explanatory note on this issue as part of our March 2024 update to the Charging Futures Forum, which can be viewed here: [Charging Futures forum | National Energy System Operator](#)

Our guidance was written in the context of the December 2024 tariff-setting period, where time restrictions meant that a licence derogation approach was most suitable in that instance. We encouraged industry to consider raising a modification proposal that would address the issue of excessive surplus residual charges on an enduring basis.

The modification proposal

DCUSA Change Proposal (DCP) 450 ('the Proposal') was raised by Eastern Power Networks ('the Proposer') on 10 February 2025. It seeks to address a defect in the CDCM where the flooring of unit rates and fixed charges at zero after revenue matching presents a limit to the possible extent of surplus residuals, which, if exceeded, can cause an incomplete set of tariffs to be produced.

This would be achieved through the inclusion of a new step in the network charging methodology, where, if the surplus residual adjustment failure is encountered, the DNO would uniformly reduce an input to the CDCM that helps determine the value of forward-looking charges. In cases where a reduction is required, this would only be to the smallest extent that allows a suite of charges to be produced. If a scaling percentage factor is used, then this is to be included in the relevant Charging Statement. The mechanism proposed in this change is therefore effectively identical to that which we suggested in our November 2024 guidance document, and which was applied as a result of subsequent directions to derogate from the charging methodology.⁶ This modification proposal was not designed to address the similar excess residual surplus issue in the Extra-High Voltage Distribution Charging Methodology (EDCM) that we had identified in our guidance.

The Proposer believes that the solution will better facilitate the First, Second, Third, and Sixth DCUSA Charging Objectives. The Proposer believes that implementation of the approach used in recent directions will mitigate complication and uncertainty in charge-setting as compared to seeking directions from Ofgem to derogate from the relevant charging methodologies and notice periods.

⁶ We have published each relevant request and direction to derogate here: [Managing the effects of surplus residual charges: derogation requests and directions | Ofgem](#)

DCUSA Parties' recommendation

In each party category where votes were cast (no votes were cast in the CVA Registrant party category),⁷ there was majority (>50%) support for the proposal and for its proposed implementation date. In accordance with the weighted vote procedure, the recommendation to the Authority is that DCP450 is accepted. The outcome of the weighted vote is set out in the table below:

DCP450 Weighted Voting (%)

	DNO ⁸ Accept	DNO Reject	IDNO/OTSO ⁹ Accept	IDNO/OTSO Reject	Supplier Accept	Supplier Reject
CHANGE SOLUTION	87%	13%	100%	0%	100%	0%
IMPLEMENTATION DATE	87%	13%	100%	0%	100%	0%

Our decision

We have considered the issues raised by the proposal and the Change Declaration and Change Report dated 15 September 2025. We have considered and taken account of the vote of the DCUSA Parties on the proposal which is attached to the Change Declaration. We have concluded that:

- implementation of the modification proposal will better facilitate the achievement of the Applicable DCUSA Charging objectives¹⁰
- directing that the modification is approved is consistent with our principal objective and statutory duties¹¹

⁷ There are currently no gas supplier parties.

⁸ Distribution Network Operator

⁹ Independent Distribution Network Operator/Offshore Transmission System Operator

¹⁰ The Applicable DCUSA Objectives are set out in Standard Licence Condition 22.2 of the Electricity Distribution Licence.

¹¹ The Authority's statutory duties are wider than matters that the Parties must take into consideration and are detailed mainly in the Electricity Act 1989 as amended.

Reasons for our decision

We consider this modification proposal will better facilitate DCUSA objectives One, Two, and Six, and has a neutral impact on the other applicable objectives.

Applicable Charging Objective One - That compliance by each DNO Party with the Charging Methodologies facilitates the discharge by the DNO Party of the obligations imposed on it under the Act and by its Distribution Licence

All Parties who voted to accept this change solution considered that Charging Objective One would be better facilitated by this code modification. They considered that the inclusion in the CDCM of a means by which to address excessive surplus residual amounts (above and beyond that which is already provided for) would mitigate against the complication, cost, and risk of a request for a direction to derogate in cases of failure of the CDCM, which are subject to individual consideration by the Authority and may result in delays to the publication of tariffs.

We consider that Charging Objective One is better facilitated by this Proposal. It is not appropriate that the ordinary and correct application of the Charging Methodologies results in a failure to produce tariffs, therefore creating dependency for some DNOs on an extraordinary process of requesting to derogate from licence obligations. The proposed modification does not change the responsibility of DNOs¹² to effectively develop the Charging Methodologies by making modifications that are necessary for the purpose of better achieving the Relevant Objectives. While we recognise that ongoing Significant Code Reviews may impact the development of network charging modifications, the experience of the surplus residual policy question should underscore the central need for expert engagement to proactively resolve foreseeable and longstanding issues.

Applicable Charging Objective Two – That compliance by each DNO Party with the Charging Methodologies facilitates competition in the generation and supply of electricity and will not restrict, distort, or prevent competition in the transmission or distribution of electricity or in participation in the operation of an Interconnector (as defined in the Distribution Licences)

¹² As under Standard Licence Condition 13 of the Electricity Distribution Licence.

Most Parties who voted to accept this change solution considered that Charging Objective Two would be better facilitated by this code modification. They considered that the inclusion of a defined process in the DCUSA would ensure that an excessive surplus residual arising in multiple network areas would be treated in a consistent manner. The inclusion of this process may also improve the foreseeability and transparency of tariffs for Users relative to the baseline. The modification may also better allow for tariffs to be published with due notice, rather than this also being subject to a direction to derogate.

One consultation respondent considered that Charging Objective Two may be detrimentally affected by this code modification. They considered that it is difficult to fully describe and assess the impacts of the solution on consumer tariffs, creating a dependency on complex interactions in the charging methodology to publish tariffs that appear unfair for some Users.

We consider that Charging Objective Two is better facilitated by this change proposal. As we have noted in previous consideration of this issue, a failure of the CDCM to produce tariffs is not a justifiable outcome. The proposed modification is an improvement by mitigating the likelihood of such an outcome in a consistent manner. The failure of the methodology to produce tariffs would undoubtedly distort competition between users of the network and likely prevent competition in its effects on the revenue recovery of both incumbent and embedded independent network operators. Licencees, and others with an interest in the charging methodologies, may wish to consider how to further improve upon the solution proposed under DCP450, including alternative or simpler approaches to scaling.

Applicable DCUSA Charging Objective Three - 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

Most Parties who voted to accept this change solution considered that Charging Objective Three would be better facilitated by this code modification, although no clear reasoning against this charging objective was provided. It may be argued that the production of a complete set of charges would satisfy this objective, as it would allow the CDCM to recover

that methodology's target revenue (interpreted here as reasonably believed to be incurred in its business, due to our price control regulation), even in cases of large surplus residual.

Conversely, enabling changes to a significant input to the CDCM's forward-looking charges (the gross asset values of the DRM) on an enduring basis may distort the incremental long-run signals produced by the cost model in ways that may not be intuitive to understand, and which may not appropriately price counterproductive behaviour (such as consumption at network peak times). Under this framing of the principle of cost-reflectivity, in cases of excessive surplus residual, the proposal would not result in charges that reflect the long-run costs of the DNO network – charges are produced which recover revenue, but with a departure from the usual assessment and attribution of costs under the cost model.

We consider this proposal is neutral against Charging Objective Three, as while it does allow for tariffs to recover expected revenue in the short run (and therefore improves against a severe failure of the methodology to produce charges), detailed reasoning was not provided for how the proposal might produce tariffs that are reflective of long-run marginal costs if used on a sustained basis.

Applicable DCUSA Charging Objective Six - That compliance with the Charging Methodologies promotes efficiency in its own implementation and administration.

All Parties who voted to accept this change solution considered that Charging Objective Six would be better facilitated by this code modification. They considered that the change proposal would positively impact upon the likelihood that relevant notice periods for tariff-setting are met. They also considered that the charge-setting process would be made more efficient by this change, due to the additional cost, time, and process required by the alternative of making requests to derogate against licence conditions or the DCUSA.

We agree with the Parties rationale for assessing that the Proposal better facilitates Charging Objective Six, and we consider that Charging Objective Six is better facilitated by the Proposal for these reasons.

Decision notice

In accordance with standard licence condition 22.14 of the Electricity Distribution Licence, the Authority hereby directs that modification proposal DCP450: "Managing the effects of surplus residual charge in the CDCM" be made.

Andrew Malley

Head of Distribution and Residual Network Charging

Signed on behalf of the Authority and authorised for that purpose