

## **Distribution Charging Structures ISG**

**7<sup>th</sup> March 2006**

### **Definition of Use of System Charges in the DUoSA**

#### ***The Issue***

At present the definition of use of system charges is contained in Clause 6 of the DUoSA. It refers to various charges, including those contained in a DNO's "Statement of Charges". This Statement should not be confused with that produced pursuant to Condition 4A of the distribution licence, albeit the Condition 4A Statement charges would invariably be embodied within the DNO's Statement of Charges. Whilst the vast majority of charges that are designated as "use of system" are tariff based a small proportion relate to specific transactions. The proposed revision to Schedule 1 of the DUoSA will place more onerous security requirements on the payment of use of system charges.

Whilst the words in all DUoSAs are identical their interpretation differs between DNOs. This is partly because the structure of the use of system charging statements differs between DNOs, and partly because different distributors take a different view towards what constitutes a use of system cost. Furthermore the recovery of some costs that are patently not use of system costs are incorporated in the use of system tariff.

Transactional charges that are legitimately use of system create difficulties when assessing the liability for security that must be provided. In general their materiality can be expected to be low but creating an internal process to assess the liability for such charges is likely to be costly and prone to failure. Indeed such is the nature of transactional charges that distribution businesses find it virtually impossible to raise invoices in accordance with the prescribed timescales, or even in some instances identify the party that is liable for the charge until after the event. If the security limit is breached because of a failure to anticipate correctly the transactional charges then it will put in jeopardy the security required for all DUoS payments.

DNOs seem prepared to waive the provision of security cover for transactional charges provided Ofgem give them an assurance that failure to secure these payments will not affect their ability to recover costs in the event of the ultimate failure of the supplier. Ofgem has been reluctant to provide this assurance.

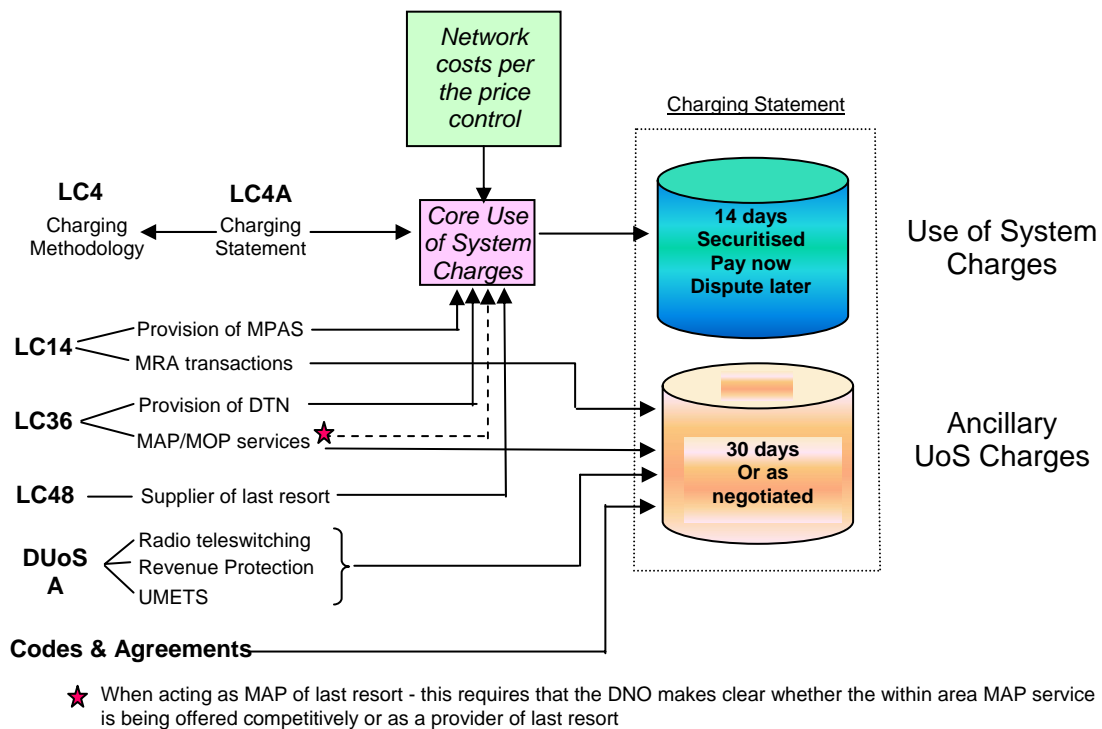
A particular problem emerges where a distributor is a Meter Asset Provider (MAP) of last resort. DNOs argue that when they act in this capacity they should be entitled to charge for this service as a use of system charge and thus apply the payment terms and security cover associated with other DUoS charges. However, few DNOs draw a distinction between the provision of meters provided within area as a competitive activity and as a provider of last resort. Hence all within area meters would tend to be covered by the security requirements of Schedule 1.

## Suggested Approach

The view has been expressed that use of system charges should be those that arise from Licence obligations. However, it is difficult to create a precise mapping from the Licence obligations to actual charges given the complexity and difference of treatment between DNOs.

To bring clarity to this confused picture a possible approach would be to insist that “use of system charges” should be defined as those charges described in the Condition 4A Statement. Obligations that distributors might have in other parts of their Licence would need to be specifically restated in the Condition 4A Statement if they were to be designated as use of system charges. Of course all charges in the 4A Statement would be backed by an appropriately described methodology approved by the Authority that would give system users the comfort that the charges had been appropriately framed.

The diagram below shows how costs incurred in the provision of a use of system service and as the result of other licence obligations could be classified as either “use of system” charges, or as charges that were ancillary to use of the distribution network. The payment arrangement in the DuoSA would differ accordingly.



## Summary

To bring clarity and uniformity to the definition of charges that can be described as “use of system” it is proposed that:

- All charges that are described by the DNO as being use of system should be listed in the Licence Condition 4A Statement, and backed by a declared methodology in the Condition 4 Statement.
- Security should not apply to transactional charges – on grounds of pragmatism
- When a meter is provided by the DNO acting as MAP of last resort then this should be made explicit in the arrangement between the DNO and the supplier.