

The Company Secretary
EDF Energy Networks plc
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*Promoting choice and
value for all customers*

Your Ref: UoS Mod 11
Our Ref: RBA/DPC/SOC
Direct Dial: 020 7901 7255

cc: Oliver Day (by email only)

12 June 2007

Dear Colleague,

Decision in relation to modification proposal UoS Mod 11 to the statement of use of system charging methodology: Removal of transition of EHV site-specific charges

On 31 May 2007, EDF Energy Networks plc ('EDF Energy') submitted to the Gas and Electricity Markets Authority (the 'Authority')¹ a proposal to modify EDF Energy's statement of Use of System (UoS) charging methodology. The proposed modification would apply to EDF Energy Networks (EPN) plc, EDF Energy Networks (LPN) plc and EDF Energy Networks (SPN) plc.

EDF Energy propose to remove the existing transitional arrangements for EHV site-specific charges, with effect from 1 October 2007. At present, annual increases in EHV UoS charges are capped at RPI level.

Having carefully considered the issues raised in the proposal, the Authority has decided not to veto the proposed modification.

This letter sets out the background to the modification proposal, explains briefly the proposed changes and sets out the reason for the Authority's decision.

Background

EDF Energy have licence obligations² to have in place as of 1 April 2005 three charging statements: the statement of UoS charging methodology, the statement of UoS charges and the connection charging methodology. The statement of UoS charging methodology outlines the method by which UoS charges are calculated. EDF Energy have a requirement to keep the methodology under review and bring forward proposals to modify the methodology that they consider better facilitate achievement of the relevant objectives³.

¹ Ofgem is the office of the Authority. The terms 'Ofgem' and the 'Authority' are used interchangeably in this letter.

² Standard Licence Conditions 4-4B.

³ The relevant objectives for the UoS charging methodology, as contained in paragraph 3 of standard licence condition 4 of EDF Energy's distribution licence are:

(a) that compliance with the UoS charging methodology facilitates the discharge by the licensee of the obligations imposed on it under the Electricity Act 1989 and by this licence;

(b) that compliance with the UoS charging methodology facilitates competition in generation and supply of electricity, and does not restrict, distort, or prevent competition in the transmission or distribution of electricity;

In April 2005, EDF Energy revised the UoS charging model to calculate charges for EHV customers. Since then, Ofgem has authorised transitional arrangements for capping annual charge increases, due to the lack of robust views on the longer-term charging model.

In its open letter of 19 October 2005⁴, Ofgem set the expectation that EHV site-specific charging methodologies would be applied in full, with no transitional relief, from no later than April 2007.

On 24 January 2007 EDF Energy Networks plc ('EDF Energy') submitted a proposal, reference UoS Mod 09⁵, to reflect the continuation of transitional arrangements and to remove the reference to the deadline of April 2007 for any interim strategy for EHV charging.

The Authority decided to veto UoS Mod 09 proposal, since it was considered that the continuation of implicit cross-subsidies across customers weakened the cost-reflectivity of the methodology. In its decision letter, the Authority also said that it expected EDF Energy to remove the ambiguous reference to April 2007.

EDF Energy Modification Proposal

EDF Energy propose to terminate all transitional arrangements for EHV site specific UoS charges. As a consequence, the EHV site-specific charging model would be fully applied for UoS charging from 1 October 2007.

Whilst broadly neutral in terms of aggregate EHV UoS revenue (which totals about £20.7 million across all three of EDF's distribution networks), this proposal results in step changes in UoS charges for a number of individual EHV customers, ranging from a 21% decrease to a 132% increase in the current monthly UoS charge. Twenty customers would experience an increase equal to or greater than 10% in the monthly UoS charge. Seven customers will benefit from a decrease equal to or greater than 10% in the monthly charge.

The Authority's decision

The Authority has considered the proposal against the relevant objectives and wider statutory duties. The change to the UoS charging methodology statement better achieves the licence objectives since the full application of the interim EHV charging model improves the degree of cost reflectivity of the current methodology.

EDF Energy launched a consultation on this matter on 20 April 2007. The Authority does not consider that the responses justify the continuation of RPI transitional arrangements.

The step changes in EHV UoS charges for a number of customers appear to result from artificial smoothing of annual increases in previous years, rather than from volatility and unpredictability of the charging model. The Authority expects licensees to review and revise their models and methodologies in cases where they could better meet the relevant objectives. The Authority accepts EDF Energy's view that the change will

(c) that compliance with the UoS charging methodology results in charges which reflect, as far as is reasonably practicable (taking account of implementation costs), the costs incurred by the licensee in its distribution business; and

(d) that, so far as is consistent with sub-paragraphs (a), (b), and (c), the UoS charging methodology, as far as reasonably practicable, properly takes account of developments in the licensee's distribution business.

⁴ 2006-07 Electricity distribution use of system EHV charges, 19 October 2005, 227/05, available at:

http://www.ofgem.gov.uk/Licensing/ElecCodes/DistCode/Mods/Archive/11802-227_05.pdf

⁵ UoS Mod 09, Transition of EHV Site Specific Charges, available at:

<http://www.ofgem.gov.uk/Networks/ElecDist/Policy/DistChrgMods/Documents1/17014-EDF%20Energy%20Networks%20UoS%20Mod%2009.pdf>

improve cost reflectivity and does not consider that a cost-reflective methodology would necessarily be more volatile.

The Authority has decided not to veto the modification to the UoS charging methodology statement.

Please contact Alberto Prandini on 020 7901 7281 if you have any queries in relation to the issues raised in this letter.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'M. Crouch', with a long horizontal flourish extending to the right.

Martin Crouch
Director, Distribution
Signed on behalf of the Authority and authorised for that purpose by the Authority