



The Company Secretary
Central Networks East plc
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Promoting choice and
value for all customers

Your ref: CNE 004

CC: John Hill (by email only)

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18 March 2008

Dear Colleague,

Decision in relation to modification proposal CNE 004: Clarification on the application of the apportionment rules

On 26 February 2008, Central Networks East plc ("CNE") submitted to the Gas and Electricity Markets Authority ("the Authority")¹ a proposal to modify its connection charging methodology.

This proposal seeks to modify the connection charging statement by providing clarification of the apportionment rules through the provision of a definition for Required Capacity and additional wording explaining how this is calculated. The Required Capacity represents the numerator of the cost apportionment factor (CAF). CNE has also added an explanation of how second comers contribute to certain existing reinforcement works.

Having considered the issues raised in the proposal, we have decided **not to veto** the proposed modification.

This letter sets out the background to the modification proposal, summarises the proposed changes and explains our decision.

Background

CNE has licence obligations² to have in place as of 1 April 2005 three charging statements: the statement of use of system (UoS) charging methodology, the statement of UoS charges and the connection charging methodology. The connection charging methodology outlines the method by which connection charges are calculated. CNE has a requirement to keep the methodology under review and bring forward the proposals to modify the methodology that it considers better achieves the relevant licence objectives.³

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 connection charging methodology, as contained in paragraph 3 of standard licence condition 4B of the licence are:

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

The apportionment rules provide a sliding scale approach to contributions from a connecting party to reinforcement costs⁴. In the case of existing customers who request an increase in supply capacity, Required Capacity can be taken to mean either the total capacity or the incremental capacity requested. The apportionment rules aim to provide a locational signal within the connection charge but equally to recognise the benefit that other users will get from the reinforcement works carried out.

CNE Modification proposal

CNE proposes to modify the connection charging methodology statement by:

- Including a definition of Required Capacity;
- Setting out how the CAF is calculated for an existing customer seeking an increased supply capacity; and
- Setting out how a second comer would contribute to certain recent reinforcements.

CNE includes a definition of Required Capacity as the capacity requested by a connecting party, or for multiple connections the total capacity required after CNE has taken account of the customer's diversity of demand. Where an existing customer requests a capacity increase, Required Capacity would be defined as the incremental capacity required by the customer.

This proposal clarifies that a second comer that makes use of assets reinforced by an initial contributor would be charged for a proportion of the reinforcement costs. This would be calculated using the apportionment rules. This policy would have effect if the second comer were to connect within five years from the time of reinforcement.

Ofgem's decision

We have considered this proposal against the licence objectives and wider statutory duties. We consider that the new definition of Required Capacity is helpful to connecting customers and aids clarity. CNE's proposal also clarifies the approach used to calculate the CAF for existing customers.

We consider that this proposal improves the cost reflectivity of connection charges by clarifying that reinforcement due to a capacity upgrade would be apportioned according to the incremental capacity increase requested, rather than the new total capacity required. We consider the use of incremental capacity to be in line with the principle that connection charges shall recover an amount for reinforcement based on a proportionate share of the costs of such reinforcement.

The proposed wording helps the customer to make a better estimate of the connection charge and understand the method used to apportion charges. We also consider that resulting connection charges would better reflect the costs incurred by the licensee in its distribution business.

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

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

⁴ The April 2004 Update paper stated that from April 2005 the connection charging apportionment rules would introduce a "shallowish" connection boundary across demand and generation, replacing deep connection charges for distributed generation and the 25 per cent rule for demand.

<http://www.ofgem.gov.uk/Networks/ElecDist/Policy/DistChrgs/Documents1/6744-April04%20Update%20Document%20SoC%20final.pdf>

We have decided **not to veto** this modification to the connection charging methodology statement.

Please contact Tom Handysides at tom.handysides@ofgem.gov.uk or on 020 7901 7289 if you have any queries relating to issues raised in this letter.

Yours faithfully,

A handwritten signature in black ink, appearing to read "Rachel Fletcher". The signature is written in a cursive style with a large, sweeping initial "R".

Rachel Fletcher

Director, Distribution

Signed on behalf of the Authority and authorised for that purpose by the Authority