



Modification proposal:	Proposal to amend the EHV charging methodologies for Designated EHV premises from April 2010 (until the introduction of the EHV Distribution Charging Methodology in April 2011) (ENW/2009/005.2)		
Decision:	The Authority ¹ directs that this proposal is not vetoed ²		
Target audience:	Electricity distributors, Suppliers, Generators and other interested parties		
Date of publication:	22 January 2010	Implementation Date:	1 April 2010

Background to the modification proposal

Electricity North West Limited (ENW) is the licensed electricity distribution network operator (DNO) for the North Western distribution services area.

DNOs are required by standard licence condition (SLC) 13 of their licences to have a methodology that sets out how they determine charges for use of their distribution systems (use of system (UoS) charges). The methodology is approved by the Authority on the basis that it achieves the Relevant Objectives³.

On 1 July 2009, new licence obligations (SLCs 13A and 50) were introduced that required DNOs to implement and maintain a common distribution charging methodology (CDCM) for their lower voltage distribution networks, i.e. the high- and low-voltage (HV and LV) networks⁴. The CDCM has now been approved by the Authority and will replace the DNO's existing lower voltage methodologies when it takes effect from 1 April 2010.

DNOs' existing methodologies for calculating UoS charges for use of the higher voltages of their networks – i.e. the extra-high-voltages (EHV) – are likely to remain in place until the end of 31 March 2011. From 1 April 2011 common EHV distribution charging methodologies⁵ (EDCMs) will replace existing EHV charging methodologies.

ENW is required by SLC 14.20 of its distribution licence to issue Notice of indicative charges that will apply from 1 April 2010. On 22 December 2009, ENW published Notice

¹ The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably in this document. Ofgem is the Office of the Gas and Electricity Markets Authority.

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

³ The 'Relevant Objectives' for the connection charging methodology, as contained in paragraph 3 of Standard Licence Condition 13 of the licence are:

- (a) that compliance with the 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 methodology facilitates competition in the generation and supply of electricity, and does not restrict, distort or prevent competition in the transmission or distribution of electricity;
- (c) that compliance with the 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 methodology, as far as is reasonably practicable, properly takes account of developments in the licensee's Distribution Business.

⁴ SLC 50 applies on and after 1 July 2009 and SLC 13A applies on and after 1 April 2010.

⁵ In accordance with our decision document entitled 'Delivering the electricity distribution structure of charges project: decision on extra high voltage charging and governance arrangements' (Ref 90/09) (please see <http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=487&refer=Networks/ElecDist/Policy/DistChrgs>), DNOs must develop and adopt either a common long run incremental cost (LRIC) or forward cost pricing (FCP) model for determining charges for customers connected to their EHV networks from 1 April 2011. These requirements are enshrined in the electricity distribution licence, see <http://www.ofgem.gov.uk/Licensing/Work/Notices/ModNotice/Documents1/Implementation%20Notice%20CLM%20proposal%2091%2009.pdf>.

of its indicative charges, which incorporates the changes made in this modification proposal.

Ofgem has reviewed each DNO's price control (DPCR5) and, on 7 December 2009, published our DPCR5 Final Proposals⁶. All DNOs have now accepted our Final Proposals in principle⁷.

The modification proposal

In the modification report submitted to Ofgem on 22 December 2009⁸, ENW explained that it proposes to modify its UoS charging methodology to facilitate the introduction of the HV/LV CDCM with the aim of minimising changes to EHV charges for the 2010/11 period. Changes to their EHV methodology are necessary because SLC 50 requires the revocation of ENW's current HV/LV methodology from their SLC 13 methodology statement. Therefore, following the revocation of their existing HV/LV methodology and the introduction of the CDCM, ENW must amend their EHV methodology to ensure it continues to operate correctly.

In particular, ENW proposes to make the following changes to its EHV methodology:

- Remove its HV/LV charging methodologies;
- Ensure that the retained EHV methodologies are clear by making necessary, albeit non-substantive, changes that ensure that they remain operable following the revocation of the existing HV/LV methodology and the introduction of the CDCM;
- Add clarificatory paragraphs to assist users of the methodology by directing the user to the CDCM for the calculation of HV/LV charges;
- Clarify the terms of its revenue reconciliation process to identify how allowed revenue is calculated and apportioned between the EHV methodologies and the CDCM; and
- Remove the Loss Adjustment Factor (LAF) Methodology.

We consider that ENW's proposal to remove its HV/LV charging methodologies is outside the scope of this decision letter⁹.

ENW additionally notes in its modification proposal that it will review Ofgem's Final Proposals and consider the comments made in relation to distributed generation (DG) that connected to its system prior to April 2005. ENW says it will bring forward further modifications where appropriate.

⁶ Ofgem's Final Proposals can be found on our website at <http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=346&refer=NETWORKS/ELECDIST/PRICECTRLS/DPCR5>.

⁷ http://www.ofgem.gov.uk/Media/PressRel/Documents1/Dp5%20acceptance_1_2010.pdf

⁸ A copy of ENW's modification report ENW/2009/005.2 can be found on the Ofgem website at <http://www.ofgem.gov.uk/Networks/ElecDist/Policy/DistChrgMods/Pages/DistChrgMods.aspx>

⁹ ENW's proposed modification illustrates how it intends to revoke its HV/LV UoS charging methodology as at 31 March 2010. These changes are made in contemplation of SLC 50.22(a) which requires ENW to revoke such parts of its UoS charging methodology used for calculating UoS charges in respect of Designated Properties (see SLC 50.10) as at that date. Such a modification request is unnecessary, however. ENW is obliged to make this revocation pursuant to SLC 50.22(a) (note: this obligation is subject only to a non-veto decision on the CDCM by the Authority). No further step is required by ENW to facilitate this revocation.

Reasons for the Authority's decision

In coming to its decision **not to veto** this proposal, the Authority has considered the proposed modification against the Relevant Objectives and the Authority's wider statutory duties¹⁰.

In summary, we have not vetoed ENW's proposal because we consider that those changes that are within the scope of this decision will better achieve relevant objective (d). The reasons for our decision not to veto ENW's proposal are set out below.

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

On 1 April 2010, ENW are obliged, subject to the Authority's approval, to implement the CDCM and to have revoked their existing SLC 13 HV/LV charging methodologies. In light of these obligations, ENW's proposal will amend its EHV charging methodology to ensure that it remains clear, accurate and transparent. In particular it will make clear that the ENW's charging methodology pursuant to SLC 13, specifically explains the calculation of EHV charges.

ENW propose to make its process of reconciling EHV demand revenue clearer. They propose to do this by making it clear that all costs used to calculate EHV demand allowed revenue are fully inflated from one regulatory year to the next and passed through to EHV demand customers. Whilst their modification report could have more effectively set out how they propose to improve the clarity of revenue reconciliation, subsequent correspondence and additional detail in their draft methodology statement has helped us understand their proposal more fully in this area.

In addition, ENW propose to make it clear that the total amount of allowed revenue to be recovered from HV/LV customers through the CDCM is calculated by subtracting EHV demand and EHV generation revenues, which are calculated in accordance with their proposed methodology statement, from the total allowed revenue that is determined in accordance with their licence. We consider that improving the clarity of the revenue reconciliation process will ensure that changes in the costs, over time, of ENW's distribution business will be properly taken into account when calculating its allowed demand revenue and that total allowed revenue is clearly apportioned between the EHV and HV/LV methodologies.

Finally, we note that ENW propose to remove their LAF Methodology and publish it in a standalone methodology statement. This is to reflect the introduction of Balancing and Settlement Code modification P216 'Audit of LLF Production'¹¹. We consider that the publication of the LAF Methodology in a standalone document is appropriate following the implementation of P216 and that the proposed words in the SLC 13 methodology will ensure that users are aware that the LAF Methodology is published separately.

We consider that all changes proposed by ENW will ensure users of their methodology continue to be able to interpret it clearly and will effectively take account of the approval of the CDCM by ensuring that ENW's EHV charging methodology remains clear. Therefore, notwithstanding the elements of this modification proposal that are outside

¹⁰ The Authority's statutory duties are detailed mainly in the Electricity Act 1989, Gas Act 1986, Utilities Act 2000, Competition Act 1998, Enterprise Act 2002 and the Energy Act 2004 as well as arising from directly effective E.C. legislation.

¹¹ Which was approved by the Authority on 24 April 2008 and implemented on 20 April 2009.

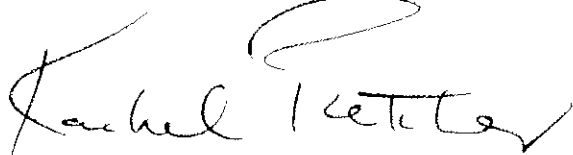
the scope of this decision letter, we consider that their proposals will better achieve Relevant Objective (d).

Additional comments

In order to facilitate the effective operation of the new open governance arrangements that will be introduced with the CDCM, we welcome proposals made by the DNOs to clarify their charging methodologies and note the importance of DNOs looking for ways to make their methodologies more accessible to users and interested parties.

In addition, whilst outside the scope of this modification decision, ENW is obliged to ensure that its methodology reflects our price control Final Proposals. We are pleased that ENW note in their modification report their intention to review our Final Proposals and to bring forward further modification proposals where appropriate. In particular, ENW will need to ensure that its methodology reflects the removal, from 1 April 2010, of the blanket exemption from charging use of system charges to DG that connected prior to April 2005.

If you have any questions relating to the issues discussed in this letter please contact Nicholas Rubin, either at nicholas.rubin@ofgem.gov.uk or on 020 7901 7176.



Rachel Fletcher

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Signed on behalf of the Authority and authorised for that purpose

