



To electricity distributors,  
generators, suppliers, customers  
and other interested parties

*Promoting choice and value for  
all gas and electricity customers*

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Dear colleague

**Decision to modify the boundary between the Common Distribution Charging Methodology (CDCM) and the EHV Distribution Charging Methodology (EDCM)<sup>1</sup> as set out in the electricity distribution standard licence conditions (SLCs)**

Distribution network operators (DNOs)<sup>2</sup> are required by their licences to have in place methodologies to calculate their charges for use of system (UoS). The CDCM for charging customers at the lower voltage levels came into effect on 1 April 2010. On 1 April 2011 the DNOs submitted to Ofgem their proposals for charging customers at the higher voltage levels (EDCM). If this methodology is approved by Ofgem, according to the DNOs' licences, the EDCM will be implemented on 1 April 2012.

The connection voltage for each customer determines whether their charges are calculated in accordance with the EDCM or CDCM. The definitions for which customers qualify for the CDCM ('designated properties') and which qualify for the EDCM ('designated EHV properties') are set out in the DNOs' licences.<sup>3</sup>

On 15 March 2011 we published an open letter consultation seeking views on changing the definitions of designated properties and designated EHV properties for Licensed Distribution Network Operators (LDNOs) – that is Independent DNOs (IDNOs)<sup>4</sup> and DNOs operating outside of their Distribution Service Area.<sup>5</sup> We also asked for views on extending the change in definitions to all customers. Our consultation followed a proposal raised on behalf of all DNOs to change the definition specifically in relation to LDNOs.

Having considered responses, we have decided that it is appropriate to amend the DNOs' licences to make it clear which charging methodology should apply to LDNOs in different circumstances. Whilst some respondents considered there was a case for applying the proposed change so that it applies to all customers connected to DNOs' networks, we do

<sup>1</sup> The CDCM is a common methodology used to calculate use of system (UoS) charges for customers connected to network operators' lower voltage (HV and LV) networks. UoS charges for customers connected to a network operator's higher voltage (EHV) networks are currently calculated in accordance with each network operators' individual EHV charging methodology. Pending approval by Ofgem, it is intended that individual EHV charging methodologies will be replaced by a common methodology, the EDCM, from 1 April 2012.

<sup>2</sup> For the purposes of this decision, and unless otherwise stated, references to a DNO are to a licensed electricity distributor that is also a Distribution Services Provider as defined in standard condition 1 of the electricity distribution licence.

<sup>3</sup> The boundary between the two UoS charging methodologies is set out in SLCs 50.10, 13A.5, 50A.11 and 13B.6 of the electricity distribution licence. The electricity distribution standard licence conditions are available at <http://epr.ofgem.gov.uk/index.php?pk=folder499235>.

<sup>4</sup> IDNOs are licensed distributors who do not have a defined distribution service area (as opposed to DNOs)

<sup>5</sup> Please see

<http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=666&refer=Networks/ElecDist/Policy/DistChrgs>

not propose to make such a change at this point. However we will consult further on this issue and, if it is appropriate and having considered the impact on UoS charges, make additional changes to DNOs' licences.

## **The DNOs' proposal**

The DNOs' proposal was driven by concerns raised by industry participants about the application of the current definitions in relation to LDNOs. The current definitions depend on the location of the Metering Point for connections within or near a primary substation. In some cases an LDNO's connection to a DNO's primary substation may not have a Metering Point<sup>6</sup>, which, using the current definitions, makes it impossible to determine whether the connection should be charged in accordance with the CDCM or EDCM. The consequence of this may be that the LDNO is unable to be assigned either a CDCM or EDCM tariff.

In other cases, for practical or safety reasons, the Metering Point at an LDNO's connection to a DNO's network may be located some distance from the actual point of connection.<sup>7</sup> Consequently, an LDNO may be charged inaccurately because the location of the Metering Point (some distance from the actual point of connection to a primary substation) suggests they should be charged in accordance with the CDCM when their actual point of connection is to the EHV network. In this circumstance being charged a CDCM UoS charge for using the HV network would be inappropriate because the LDNO is only using the DNOs' EHV network.

The DNOs published a consultation in February 2011 that sought general views on their development of the EDCM as it relates to LDNOs.<sup>8</sup> The consultation set out that the electricity distribution licence may need to be amended to clarify the definitions. In their consultation the DNOs set out an "interim" set of definitions:

*"The following types of LDNO distribution systems would qualify for discounts calculated using the extended method M model [i.e. qualify as an Designated EHV Property]:*

- (a) LDNO Distribution Systems connected to the licensee's Distribution System at 22 kilovolts or more; and*
- (b) LDNO Distribution Systems connected directly to substation assets that form part of the licensee's Distribution System at 1 kilovolt or more and less than 22 kilovolts where the primary voltage of the substation is 22 kilovolts or more and where the asset ownership boundary is physically located at the same substation."*

## **Our consultation**

In our open letter consultation, we sought views on modifying the definitions for Designated Properties in accordance with the DNOs' proposed wording (see above). We also sought views on whether a revised definition using ownership boundary rather than Metering Point should apply to all customers' connections, as opposed to just LDNO:DNO connections.

We set out our initial view that a change to the licence definition is needed for LDNOs for the reasons noted above. We also said that using the ownership boundary as a point to determine if LDNOs should qualify for CDCM or EDCM tariffs was appropriate. The ownership boundary is appropriate because the DNO charges are intended to reflect the assets used by the DNO in providing distribution services to LDNOs.

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<sup>6</sup> Following the introduction of portfolio billing of LDNOs with the CDCM on 1 April 2010 it is no longer necessary to have equipment in place to measure flows of electricity across the DNO/IDNO boundary for billing purposes.

<sup>7</sup> A similar argument may be made in the case of network users other than LDNOs. However, we understand that this is much more likely to be the case for network to network connections.

<sup>8</sup> Please see <http://energynetworks.squarespace.com/edcm-file-storage/6-consultations/06-consultation-on-ldno-charging-feb-2011/>

We noted in our consultation that there was the potential for the change in boundary to impact on charges for end customers because changes to LDNO charges would affect the amount of revenue that would have to be recovered from them. However we expect the impact on UoS charges because of the change in boundary definition to be very small and only affect a small number of LDNO connections. This is because there are only a small number of LDNO connections close to primary substations.

We considered that a more comprehensive change to the boundary, for example one that would apply the asset ownership test to all customers, was not necessary at this time as, unlike for LDNOs, a workable definition for these customers is already in place. Further we stated that we have recently consulted and undertaken a full impact assessment on the definition of the boundary and its implementation. We set out that we did not think it would be appropriate to change this without a further consultation and impact assessment.

We received eight responses to our consultation. Six of these were from DNO representatives and two were from IDNO representatives.<sup>9</sup>

In general all respondents were supportive of a change to the boundary definition for LDNOs. There were differences in opinion between respondents regarding whether the change should be made for all customers and also whether, if the change were to be made for LDNOs only, we should make the change prior to consulting on its extension to all customers.

All respondents recognised the need to clarify the definitions in order to take account of the particular circumstances of LDNOs and the consequences of maintaining the current definitions. For example, one respondent considered that the current definition may result in undue discrimination against (or in favour of) an LDNO. This is because the current definition may lead to the LDNO paying a charge in respect of assets it does not actually use (or avoiding a charge for assets that it does use).

Respondents also considered that the use of the ownership boundary is appropriate in the absence of a Metering Point. One respondent argued that it may be appropriate for the ownership boundary to be used in relation to all customers because metering may, for safety or cost reasons, be located some distance from the actual physical boundary between the DNO and the connectee.

There were mixed views in relation to whether a change in the definition should be limited to LDNOs only. That is, three respondents supported limiting it to LDNOs only and four respondents supported applying the definition to all distribution systems. In relation to applying the revision to LDNOs only, one respondent stated that the issue driving the need for change is limited to LDNOs only and so any change should be restricted to LDNOs. Respondents who support a change in definition applying to all distribution systems considered that it was appropriate because the circumstance it corrects could apply to any distribution system (or customer) and the proposed definition would then apply consistently to all.

There were also mixed views in relation to whether we should delay our decision and consult on applying the proposed revision to all customers. Of those who commented on this issue, all respondents considered that there would be value in further considering whether a change in the definition of designated properties should apply to all customers. Three of those respondents considered we should make a change now in relation to LDNOs only and review the issue in relation to all customers at a later date, for example as part of our consultation of the DNOs' proposed EDCM. One respondent said that we should consult and make a change for all if there was time to do so before DNOs publish indicative charges in December 2011. If there was not sufficient time, the respondent said that we should make the change for LDNOs only and review the issue in due course. One respondent

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<sup>9</sup> We have published all non-confidential responses on our website. Please see <http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=666&refer=Networks/ElecDist/Policy/DistChrgs>

considered we should delay any change until we have reviewed its application to all customers. Another respondent considered that to the extent that the current definition is flawed, we should review its application in relation to all customers. This respondent also noted that if we chose to delay making a change until after the EDCM is approved, we should commit to reviewing this issue within a set time period.

## **Our decision**

We have decided that it is appropriate to modify the DNOs' licences so that the definitions in relation to designated properties are updated to reflect specific circumstances that may apply in relation to LDNOs only. Furthermore we have decided to implement these changes as soon as possible.

We have decided to make the change primarily because the current definition of designated properties does not work for LDNOs connected close to a primary substation. Without this change it is possible that the licensee is unable to determine whether LDNOs connected to a primary substation are charged in accordance with the CDCM or EDCM. We also think that the change will be beneficial because it is commonplace for an LDNO point of connection to be located a significant distance from the physical boundary between the DNO and LDNO. This could mean that the LDNO could be charged in accordance with a methodology that does not accurately reflect their point of connection or the DNO's assets they use.

In order to resolve this deficiency in the current drafting of the licence we propose to modify SLCs 13A and 50A using an approach similar to that which the DNOs proposed as their interim solution.<sup>10</sup> That is to use the ownership boundary as opposed to the Metering Point to determine whether an LDNO is charged in accordance with the CDCM or EDCM. We consider that using the ownership boundary is appropriate because the charging methodologies calculate charges for use of network companies' assets and for an LDNO:DNO connection the ownership boundary is the literal boundary between the two networks. Therefore UoS charges will be calculated in relation to the LDNO's actual use of the DNO's network. Our proposed changes to the SLCs are set out in detail in the annex to the statutory consultation we have published alongside this decision letter.

We consider it appropriate that we make this decision prior to our decision on the EDCM rather than, as some parties have suggested, to delay the decision. This is because the EDCM is dependent on a change being made so that unmetered LDNO can be assigned tariffs. To delay the decision on this necessary change would introduce unnecessary uncertainty into the process for making our decision on the EDCM.

We note that a majority of respondents supported applying the proposed definitions of designated properties to all customers. We consider that it would be appropriate to properly consult on the broader application of a definition of designated properties based on ownership boundary before formally seeking to modify DNOs' licences. The licence currently adequately determines whether customers other than LDNOs are charged in accordance with the CDCM or EDCM. Furthermore the current licence drafting is a consequence of recent consultation, impact assessment and a licence modification. Whilst it may be that the licence's application in relation to all customers could be improved, we consider that it is adequate for the time being.

In the meantime we consider it is necessary to have a working definition in place for LDNOs in time for the EDCM to take effect.

## **Statutory consultation**

We are publishing a statutory consultation notice today alongside this decision letter, setting out the proposed licence modifications that are required to implement our decision. Electricity distribution licence holders have 28 days to decide whether or not to accept the

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<sup>10</sup> See above

proposed modifications; the deadline for representations is 31 August 2011. If accepted, we will seek to implement the proposed modifications to coincide with a decision to approve the EDCM.

The 2009 Electricity Directive<sup>11</sup> requires that a party affected by a decision of a regulatory authority be provided with a suitable mechanism for appealing against that decision. The United Kingdom is in the process of implementing that requirement. If you wish to exercise such a right of appeal against our decision in this case, please notify us in your representations.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'Rachel Fletcher', is written over a light grey rectangular background.

Rachel Fletcher

**Partner, Distribution**

Signed on behalf of the Authority and authorised for that purpose

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<sup>11</sup> Directive 2009/72/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in electricity and repealing Directive 2003/54/EC