

RIIO-ED1: Informal consultation on slow-track licence drafting – Charge Restriction Conditions

Consultation

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Contact: Clothilde Cantegreil

Team: RIIO-ED1

Tel: 020 7901 3195

Email: clothilde.cantegreil@ofgem.gov.uk

Overview

We are consulting on the main proposed changes to the Charge Restriction Conditions (CRCs) required to implement the RIIO-ED1 price control settlement, including a developed draft of the proposed Price Control Financial Handbook. Unless specified, these conditions will apply to all electricity distribution network operators (DNOs), except the four licensees of Western Power Distribution (WPD). These conditions will apply from 1 April 2015.

WPD's price control was finalised in May 2014. The remaining companies submitted revised business plans in March 2014. On 30 July 2014 we published our proposed settlements (draft determinations) for the remaining companies. This document consults on the licence changes that will enable us to implement the settlements we will set out in the final determinations for the companies in November. We proposed additional bespoke provisions for certain DNOs in our draft determinations. These are being developed separately and are not included in this consultation.

Context

RIIO-ED1 is the first electricity distribution price control to reflect the new RIIO (Revenue = Incentives + Innovation + Outputs) model. In the RIIO-ED1 price control review we will set the outputs that the 14 electricity DNOs need to deliver for their consumers and the associated revenues they are allowed to collect. The RIIO-ED1 review covers an eight-year price control from 1 April 2015 to 31 March 2023.

Western Power Distribution's (WPD) price control was settled early and the required modifications to WPD's licences were finalised in May 2014 (apart from those relating to the close out of current price control schemes).¹ We also modified a number of the Standard Licence Conditions (SLCs)², which apply to all DNOs and support the operation of the price control over its duration.

We are now consulting on the main changes to the remaining DNOs' Charge Restriction Conditions (CRCs) to implement their individual settlements, including a developed draft of the proposed Price Control Financial Handbook. These include our proposals for provisions for the close out of current price control schemes, which we propose also to apply to WPD's licensees. We proposed additional bespoke provisions for certain DNOs in our Draft Determination. These are being developed separately and are not included in this consultation.

Associated documents

Documents published alongside this consultation

- Supplementary annex 1: Draft RIIO-ED1 slow-track CRC licence changes
- Supplementary annex 2: ED1 Price Control Financial Handbook
- Supplementary annex 3: Response template

Other relevant documents

- [RIIO-ED1: Draft determinations consultation for the slow-track electricity distribution companies](#)
- [Strategy decision for RIIO-ED1 – Overview](#)
- [RIIO ED1 Glossary](#)

¹ RIIO-ED1: Modifications to special conditions of the electricity distribution licences held by the four licensees owned by Western Power Distribution plc (WPD) - <https://www.ofgem.gov.uk/publications-and-updates/riio-ed1-modifications-special-conditions-electricity-distribution-licences-held-four-licensees-owned-western-power-distribution-plc-wpd>

² RIIO-ED1: Modifications to the standard conditions of the electricity distribution licences - <https://www.ofgem.gov.uk/publications-and-updates/riio-ed1-modifications-standard-conditions-electricity-distribution-licences>

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Executive summary

The price control settlement is implemented through the licence for the DNOs. The licence comprises Standard Licence Conditions (SLCs), which are applicable to all DNOs, and Charge Restriction Conditions (CRCs), which are unique to each DNO.

We are consulting on the main draft CRCs for all slow-track DNOs. The CRCs for the slow-track DNOs were developed based on the modifications to WPD's special conditions³ and follow the same structure.

This consultation also includes a draft of Section 1 of the ED1 Price Control Financial Handbook (handbook). This sets out the methodologies that will be followed during RIIO-ED1 to update licensees' revenue allowances for RIIO-ED1 policy-related schemes. Finally, we are consulting on the legacy price control adjustments for the regulatory years before 2015-16, including a developed draft of the relevant chapters of the handbook. This will apply to all licensees, including WPD.

We proposed additional bespoke provisions for certain DNOs in our draft determinations. These are being developed separately and are not included in this consultation.

We are also conducting a parallel consultation covering any changes to the SLCs which could not be finalised in May 2014.

In December 2014, we will conduct the requisite 28-day statutory consultations, which will include the additional conditions referred to above which are outside this consultation and any other changes which become necessary to implement Final Determinations. These will cover the residual changes to the SLCs and the slow-track companies' CRCs. We will publish our licence modification decisions in February 2015. Licence changes will come into force from 1 April 2015.

³ RIIO-ED1: Modifications to special conditions of the electricity distribution licences held by the four licensees owned by Western Power Distribution plc (WPD) - <https://www.ofgem.gov.uk/publications-and-updates/riio-ed1-modifications-special-conditions-electricity-distribution-licences-held-four-licensees-owned-western-power-distribution-plc-wpd>

1. Introduction

Chapter summary

A guide to the purpose of the document. It also provides an overview of our approach to licence drafting and our next steps in the licence development process.

Purpose of this document

1.1. In this document we set out our current thinking and request your views on:

- The updated timetable for RIIO-ED1 licence development.
- The proposed changes to the Charge Restriction Conditions (CRCs) for all slow-track DNOs. We are consulting on changes to those CRCs which are common to all DNOs. Company-specific changes will be dealt with separately along with any additional changes which become necessary to implement Final Determinations.
- Part 1 and Part 2 of the ED1 Price Control Financial Handbook for the slow-track DNOs. This describes the methodologies that will be followed to update licensees' revenue allowances for RIIO-ED1 policy-related schemes.
- CRC 3A and Part 3 of the ED1 Price Control Financial Handbook for all licensees, including the WPD licensees. These describe the methodologies that will be followed to close out DPCR5 schemes during RIIO-ED1. As part of this, we are proposing changes to some of the methodologies found in the DPCR5 final proposals⁴. This is because RIIO-ED1 introduces an annual iteration process which can be used to close out DPCR5 schemes.

1.2. This consultation seeks your views on whether our proposed licence and handbook drafting reflects the policy position detailed in the strategy decision and in the draft determinations published for all slow-track DNOs.⁵

1.3. We have also published 'RIIO-ED1: Second informal consultation on licence drafting – Standard Licence Conditions', which we are consulting on in parallel. It covers residual changes to the Standard Licence Conditions (SLCs) which could not be finalised in May 2014. These will apply to all DNOs.

1.4. We aim to publish the required licence modifications in February 2015. These will bring the relevant licence conditions (both SLCs and CRCs) into force from 1 April 2015.

⁴ Electricity Distribution Price Control Review Final Proposals - <https://www.ofgem.gov.uk/publications-and-updates/electricity-distribution-price-control-review-final-proposals>

⁵ Strategy decision for RIIO-ED1 – Overview - <https://www.ofgem.gov.uk/publications-and-updates/strategy-decision-riio-ed1-overview>
RIIO-ED1: Draft determinations consultation for the slow-track electricity distribution companies - <https://www.ofgem.gov.uk/publications-and-updates/riio-ed1-draft-determinations-consultation-slow-track-electricity-distribution-companies>

Types of licence conditions

1.5. There are two different types of licence condition in electricity distribution licences - SLCs and CRCs.

Standard Licence Conditions (SLCs)

1.6. The SLCs set out the duties and obligations applicable to all holders of an electricity distribution licence. They are shared conditions. The SLCs are grouped into two sections. Section A applies to all Electricity Distributors, both DNOs and Independent Distribution Network Operators (IDNOs), while Section B applies only to DNOs. SLCs do not feed into the determination of the DNOs' allowed revenue – this is done through the CRCs.

Charge Restriction Conditions (CRCs)

1.7. CRCs apply specifically to each licensee (ie each DNO has its own set). However, certain conditions may be similar and, in some cases, identical across the DNOs. Broadly, CRCs place obligations on companies that have an impact on their allowed revenue.

Approach to licence drafting for RIIO

Licence Drafting Working Group

1.8. We created a Licence Drafting Working Group (LDWG) comprising of members of the Ofgem team and DNO representatives. This group has met regularly to review and develop the licence conditions and handbook. We also established a working group with the DNOs to develop the ED1 Price Control Financial Model. The DNOs have been very committed to this process and have provided constructive feedback.

Fast-track modifications

1.9. We developed a full set of CRCs (minus provisions dealing with DPCR5 close out), Section 1 of the ED1 Price Control Financial Handbook and the ED1 Price Control Financial Model for WPD's licensees to implement the fast-track settlement. Following two consultations we modified their licences on 21 May 2014 to introduce these provisions.⁶ The CRCs and Section 1 of the handbook which we are consulting

⁶ RIIO-ED1: Modifications to the standard conditions of the electricity distribution licences - <https://www.ofgem.gov.uk/publications-and-updates/riio-ed1-modifications-special-conditions-electricity-distribution-licences-held-four-licensees-owned-western-power-distribution-plc-wpd> and Modifications to special conditions of the electricity distribution licences held by the four licensees owned by WPD - <https://www.ofgem.gov.uk/publications-and-updates/riio-ed1-modifications-special-conditions-electricity-distribution-licences-held-four-licensees-owned-western-power-distribution-plc-wpd>

on in this document are for the most part identical to those in WPD’s licences. We show where they differ and why in this document.

Licence structure

1.10. Where possible, we have looked to incrementally adapt the CRCs currently in force for DPCR5 in a way that retains their look and style. However, implementing new policy for RIIO-ED1 means that we are proposing some significant changes to the content of the CRCs. These include:

- amendments to current conditions
- the removal of current conditions
- the introduction of completely new conditions.

1.11. Given the extensive number of proposed changes to the CRCs, we believe that retaining the current licence numbering has no benefit. We propose to change the numbers of all CRCs that are retained for RIIO-ED1. We also propose to group CRCs into chapters to ensure that similar types of conditions are together. For example, we have created a specific chapter to hold all the variables that may be adjusted through the annual iteration of the Price Control Financial Model.

1.12. The introduction of chapters will also help retain a coherent structure in the event that any CRCs are added or removed during the RIIO-ED1 price control period.

Proposed new structure

1.13. Our proposed new structure, including new numbering and condition names, is outlined in Appendix 2. The table shows:

- conditions that are new for RIIO-ED1
- current DPCR5 conditions that are being changed
- the number, if applicable, of the current DPCR5 condition
- which of the current DPCR5 conditions we propose to remove.

1.14. Appendix 2 also highlights if a licence condition governs an ‘associated document’. Associated documents are more detailed guidance or instruction documents which are given legal authority via the licence.

1.15. Chapter 4 contains further information on the CRC associated documents for RIIO-ED1.

1.16. While CRCs apply to each licensee individually, we seek to maintain common content and numbering across all licensees wherever possible. With this document, we are consulting on licence conditions common to all DNOs.

Timetable for RIIO-ED1 licence development

1.17. The timetable for making the necessary RIIO-ED1 CRC and SLC licence changes is set out below, including for the slow-track companies.

Table 1: Timetable for RIIO-ED1 licence development

Stage	Date
Charge Restriction Conditions	
<i>Slow-track companies and DPCR5 close-out for all companies</i>	
Informal licence drafting consultation	September 2014
28 day statutory licence modification consultation and notices published	December 2014/ January 2015
Licence modification decision and modifications published	February 2015
Licence changes come into force	1 April 2015
Standard licence conditions	
<i>All Electricity Distributors: RIIO-ED1 remaining SLC modifications</i>	
Informal licence drafting consultation	September 2014
28 day statutory licence modification consultation and notices published	December 2014/ January 2015
Licence modification decision and modifications published	February 2015
Licence changes come into force	1 April 2015


Responding to this consultation

1.18. The proposed CRCs are set out in 'Supplementary annex 1: Draft RIIO-ED1 Slow-track CRC licence changes'. The proposed Price Control Financial Handbook is set out in 'Supplementary annex 2: ED1 Price Control Financial Handbook'. We welcome comments on the proposed drafting and the specific questions in this consultation.

1.19. Please use the Response Template (Supplementary annex 3) to provide any substantive feedback on each individual licence condition. Ensure that any points raised in the cover letter are also made in the Response Template. Minor points on the individual licence drafts (eg formatting and drafting improvements) can be supplied in a tracked-change version of the relevant licence condition.

Structure of this document

1.20. The remainder of this document is structured as follows:



RIIO-ED1: Informal consultation on slow-track licence drafting – Charge Restriction Conditions

- Chapter 2 details the proposed change to each CRC, the reason behind the change and the intended effect of each
- Chapter 3 outlines the associated documents that are being created for RIIO-ED1 through the changes to the licence
- Chapter 4 provides a brief overview of the Price Control Financial Handbook
- Chapter 5 introduces the changes that we have made to the methodologies for closing out DPCR5 schemes and explains our reasons behind this change.

1.21. Alongside this document we have also published the following Supplementary annexes:

- Supplementary annex 1: Draft RIIO-ED1 slow-track CRC licence changes
- Supplementary annex 2: ED1 Price Control Financial Handbook
- Supplementary annex 3: Response template

2. Proposed changes to the CRCs

Chapter Summary

Our proposed changes to the CRCs for all slow-track DNOs.

Question 1: Do you have any views on the proposed changes to the CRCs? The draft licence conditions are found in supplementary annex 1.

Question 2: Do you have any views on the reasons and effects for the licence changes proposed in this consultation?

Types of CRC change

2.1. The proposed licence modifications fall into three broad categories:

- amendment to a current CRC
- removal of a CRC that was required for DPCR5, but not for RIIO-ED1
- new CRC for RIIO-ED1.

2.2. Where we refer to the 'current' condition, or what a condition 'currently' refers to, we are referring to the condition in the current (DPCR5) licence.

2.3. Unless otherwise specified, the conditions are identical to those for WPD's licensees and will apply to all slow-track DNOs.

Amendment to current CRCs

2.4. We have proposed amendments to some of the current CRCs to reflect the new RIIO-ED1 policy and ensure that they remain operational under the RIIO regulatory framework.

2.5. Some amendments to CRCs are relatively minor, while others are substantive. Where the amendments are minor, we have shown them in tracked changes made to the current DPCR5 condition. Where the changes are numerous and substantive, we have not shown them in tracked changes.

Removal of CRCs from licence

2.6. We propose that some DPCR5 CRCs should no longer exist for RIIO-ED1. This is typically because a change in policy has led to an incentive no longer being applicable.

New CRCs for RIIO-ED1

2.7. We have proposed some new CRCs. This is to reflect new policy being introduced for RIIO-ED1.

Draft RIIO-ED1 licence conditions

2.8. We have set out the proposed CRC licence changes in 'Supplementary annex 1: Draft RIIO-ED1 Fast-track CRC licence changes'. This only includes the proposed CRCs which are common to all DNOs. The remaining company-specific CRCs are still being developed

Reasons and effects for proposed CRC changes

2.9. We have set out the reasons and effects for the proposed CRCs in the order they appear in our proposed new structure of the licence for RIIO-ED1 (see Appendix

Chapter 1

CRC 1A. Overview of Part 4

Type of change: Amendment to existing CRC

Current number: CRC 1

Current name: Overview of Part 4

2.10 The reasons for the changes to modify CRC 1 of the current licence are:

- to ensure that CRC 1A accurately describes the revised scope and structure of Part 4 of the RIIO-ED1 licence
- to remove from CRC 1A provisions which would duplicate other provisions contained in Part 4. This is to avoid the possibility of inconsistencies and confusion.

2.11 The effects of the modifications are to:

- renumber the condition as CRC 1A
- set out the scope of Part 4
- add a new part to the condition, which describes the structure of Part 4
- add a new part to the condition to set out the acronyms used throughout the CRCs to refer to the licensed electricity distributors
- amend the definition of Charge Restriction Condition, so that they are now defined by reference to their location in Part 4
- no longer include a description of how the CRCs may be modified.

CRC 1B. Interpretation of Part 4

Type of change: Amendment to existing CRC

Current number: CRC 2

Current name: Definitions for the Charge Restriction Conditions

2.12 This condition modifies CRC 2 of the current licence, which sets out defined terms and their definitions for the Charge Restriction Conditions. The reasons for this new condition, including differences with the current condition, are:

- to incorporate all overarching provisions relating to the interpretation of Part 4 within one condition for ease of reference
- to introduce new terms and their definitions needed for the modifications referred to below
- to remove redundant defined terms and their definitions no longer required because of the modifications referred to below
- to amend some current defined terms and their definitions
- to correct references to outdated legislation and cross-references to other licence conditions consequent to the modifications referred to below.

2.13 The effects of the modifications are:

- to renumber the condition to CRC 1B and to amend its title
- to update the defined terms and their definitions.

Chapter 2

CRC 2A. Restriction of Allowed Distribution Network Revenue

Type of change: New condition, which replaces three current conditions

Current conditions: CRC 3, 5 and 14

Current names: Restriction of Distribution Charges: Use of System Charges, Restriction of Distribution Charges: non-generation incentive revenue adjustment, and Distribution Charges: supplementary restrictions

2.14 This new condition calculates the allowed distribution network revenue the licensee can recover from customers, in each year of the price control period. This condition totals variables populated by other CRCs. It also sets out the calculation of the price index adjustment factor used throughout the licence and the correction factor (K) for the treatment of over/under recovered revenue.

2.15 This condition replaces the current conditions CRC 3, CRC5 and CRC 14. CRC 3 set out the restriction of distribution charges: use of system charges; CRC 5 set out the restriction of distribution charges: non-generation incentive revenue adjustment and CRC 14 set out the calculation of the correction factor (K). For RIIO-

ED1 we consider that it is efficient to combine these conditions into a single condition, and that we can do this without making significant changes to the intent of the current conditions.

2.16 This condition also gives effect to:

- the new annual iteration process of the price control financial model. This process creates a term known as MOD_t which is included in the calculation of allowed distribution network revenue.
- aspects of our October 2012 decision to mitigate network charging volatility, and its effects, by modifying the way the correction factor (K) operates.⁷ We propose that it operates with:
 - a two year lag. DNOs will transition from the current one year lag; this transition will vary by licensee, based on a bespoke process to close out any DPCR5 under/over recoveries including any effects of the government’s December 2013 measures to reduce energy bills
 - an increased band in which no penalty applies (to take account of the fact that changes to charges are no longer applicable on dates other than 1 April)
 - a process for direction, by the Authority, of an alternative penalty interest rate (PRT)
 - a further penalty to be applied for persistent over/under recovery.
- our decision to change the way the price indexation adjustment factor is calculated.⁸ The effect of applying this decision is the creation of a new price indexation adjustment factor called $RPIF_t$ and a true up to account for the difference between forecast and actual inflation, known as TRU_t .

CRC 2B. Calculation of Allowed Pass-Through Items – terms common to all DNOs

Type of change: Amendment

Current number: CRC 4

Current name: Restriction of Distribution Charges: calculation of the Allowed Pass-Through Items

2.17 The purpose of this condition is to calculate the pass-through costs that the licensee is allowed to recover from customers.

2.18 There are no significant changes to the broad intent of the current condition. We have made changes in the following areas:

⁷ Decision in relation to measures to mitigate network charging volatility arising from the price control settlement (Oct 2012) - <https://www.ofgem.gov.uk/ofgem-publications/50572/cvdecision.pdf>

⁸ Decision on the RPI indexation method to apply to allowed revenues in the forthcoming RIIO price controls (T1 and GD1) and the TPCR4 rollover (July 2011) - <https://www.ofgem.gov.uk/ofgem-publications/53813/rpi-issue-decision-letter.pdf>

- several pass-through terms have been added and removed from the Principal Formula set out in our Strategy decision, of the current condition to reflect the policy set out in our Strategy decision for the RIIO-ED1 electricity distribution price control (Strategy decision)
- changes have been made to reflect the Authority’s decision on measures to mitigate charging volatility, by introducing a two year lag to the adjustments.⁹

2.19 The effect of these changes is to continue to allow licensees to pass-through a defined list of costs to customers and reduce charging volatility by introducing a two-year lag.

CRC 2C. Broad Measure of Customer Service Adjustment

Type of change: Amendment

Current number: CRC 8

Current name: Adjustment of the licensee’s revenues to reflect quality of service performance

2.20 This is an amendment to the current CRC 8, which calculates the revenue-adjusting term that reflects the licensee's performance against the Broad Measure of Customer Service.

2.21 The modifications rename and renumber the current condition and replace the current wording with a new condition which:

- amends the structure
- removes the overall component of the Customer Satisfaction Survey
- updates the target/maximum reward/maximum penalty for the Customer Satisfaction Survey
- introduces the proportion of unsuccessful calls into the DNO’s performance under the interruptions element of the Customer Satisfaction Survey
- updates the weightings of the complaints metric
- updates the target/maximum penalty score for the complaints metric.

2.22 The condition also establishes the Stakeholder Engagement Incentive Guidance, which provides information on the governance arrangements of the stakeholder engagement incentive. This is an associated document to the licence.

2.23 The effect of these modifications is to enable the licensee to recover revenue streams that are consistent with our Strategy Decision.

⁹ Decision in relation to measures to mitigate network charging volatility arising from the price control settlement (Oct 2012) - <https://www.ofgem.gov.uk/ofgem-publications/50572/cvdecision.pdf>

2.24 We have also amended the formula in paragraph 2C.15, compared to the formula specified in the WPD’s licence. The effect of this change is that if a DNO scores above the target level of satisfaction, but has a high proportion of unsuccessful calls, it will not be penalised more than the maximum penalty for the supply interruptions element of the customer satisfaction survey. The reason for the change is to make it consistent with our desired policy intent. We will make this correction to WPD’s licence at a later date.

CRC 2D. Adjustment of licensee’s revenues to reflect interruptions-related quality of service performance

Type of change: Amendment

Current number: CRC 8 (excluding Part D)

Current name: Adjustment of licensee’s revenues to reflect quality of service performance

2.25 The modifications rename and renumber the current condition and replace the current wording with a new condition. The new condition retains much of the current content, but includes the following changes (for the following reasons and with the following effects):

- separation of the planned and unplanned elements of the targets for the number of customer interruptions so as to provide clarity to stakeholders on the licensees’ performance
- updating targets for number and duration of customer interruptions, so as to reflect industry performance since targets were set in DPCR5
- updating the threshold values for both types of exceptional events to reflect more recent data
- amending the revenue exposure terms and the incentive rates to reflect the Strategy Decision.

CRC 2E. Incentive on Connections Engagement

Type of change: New condition

2.26 The reason for introducing this new condition is to calculate the revenue-adjusting term that reflects the licensee’s performance as part of the Incentive on Connections Engagement, which was set out as part of the Strategy Decision.

2.27 The effect of this new condition is to enable the licensee to incur penalties where it fails to meet the criteria in relation to its connections activities set out in the Incentive on Connection Engagement Guidance. The Incentive on Connection Engagement Guidance is an associated document to the licence.

CRC 2F. Time to Connect Incentive

Type of change: New condition

2.28 The reason for introducing this new condition is to calculate the revenue-adjusting term that reflects the licensee's performance against our new Time to Connect Incentive, which was set out as part of the Strategy Decision.

2.29 The effect of this new condition is to enable the licensee to recover revenue streams for the RIIO-ED1 Time to Connect Incentive.

CRC 2G. The Losses Discretionary Reward

Type of change: New condition

2.30 The reason for introducing this new condition is to provide the revenue-adjusting term that reflects any additional revenue the Authority may, at its discretion, award the licensee under the Losses Discretionary Reward, which was set out as part of the Strategy Decision.

2.31 The effect of this new condition is to enable the licensee to collect revenue rewards awarded under the Losses Discretionary Reward. This condition also introduces the Losses Discretionary Reward Guidance Document, which will set out the criteria that needs to be met by the licensee to be eligible for any reward.

CRC 2H. The Network Innovation Allowance

Type of change: New condition

2.32 In the Strategy Decision we outlined the introduction of an innovation stimulus. One component of the innovation stimulus is a Network Innovation Allowance (NIA). The NIA is a set allowance of funding for the licensees to spend on smaller-scale innovative projects with potential financial benefits to consumers. The purpose of this condition is to establish the NIA arrangements.

2.33 The effect of this condition is to establish arrangements, known as the Network Innovation Allowance. This condition sets out:

- that the detailed regulation, governance and administration of the NIA will be set out in the NIA governance document, and that this document should be complied with as if it formed part of the licensee's licence (the NIA governance document is an associated document to the licence)

- the percentage of each licensee’s base revenue it can spend on innovative projects that conform to the NIA governance document, this being provided on a “use it or lose it” basis
- the scope of the NIA governance document
- the change control processes for the NIA governance document
- that only NIA expenditure that conforms to the requirements of the NIA governance document will be considered eligible.

CRC 2I. Not used

Type of change: New condition

2.34 The reason for introducing this condition is to provide the licensee with clarity that that this condition is not used in the pack of their CRCs.

2.35 The introduction of this condition has no effect on any party

CRC 2J. Low Carbon Networks Fund

Type of change: Amendment

Current number: CRC 13

Current name: Low Carbon Networks Fund

2.36 In the Strategy Decision we outlined the introduction of an innovation stimulus and the removal of the Low Carbon Networks (LCN) Fund.

2.37 The LCN Fund consists of a First Tier and a Second Tier. As outlined in the Strategy Decision, the First Tier of the LCN Fund will be replaced by the NIA. The Second Tier will be replaced by the electricity Network Innovation Competition (NIC). The final Second Tier competition in the LCN Fund will take place in 2014 with funding being transferred to successful licensees in 2015.

2.38 In addition, a number of Second Tier projects awarded funding during DPCR5 will continue into RIIO-ED1. We may also award some discretionary reward funding beyond April 2015 for exceptional projects, which were awarded funding during DPCR5. There will be no First Tier projects continuing into RIIO-ED1, as these will need to be registered under the NIA.

2.39 The modifications rename and renumber the current condition and replace the current wording with a new condition. The new condition retains much of the current condition, but includes the following changes which enable the Authority, within the context of RIIO-ED1 to:

- continue monitoring ongoing Second Tier projects
- retain the ability to halt projects and disallow expenditure

- disallow any expenditure under the First Tier which may have been misspent during DPCR5.

2.40 The effect of the modified condition is to continue the arrangements for the Second Tier of the LCN Fund and maintain the eligibility requirements for the First Tier of the LCN Fund (while there will be no First Tier projects this will continue to allow us to claw back funding if we discover it has been ineligible). This includes:

- the First Tier funding mechanism, which outlines the requirements for First Tier projects
- the Second Tier and Discretionary Funding Mechanism, which outlines the circumstances under which the licensee will receive funding and the circumstances under which the licensee must return money
- maintaining that the regulation, governance and administration of the LCN Fund will be detailed in the LCN Fund governance document
- maintaining that the licensee must comply with the LCN Fund governance document as if it formed part of the licence
- maintaining the procedures for issuing and revising the LCN Fund governance document.

2.41 The LCN Fund governance document is an associated document to the licence.

CRC 2K. Margins on licensee's Connection Activities

Type of change: Amendment

Current number: CRC 12

Current name: Licensee's Connection Activities: Margins and the development of competition

2.42 The reason for modifying the current condition is to update the licence condition following the outcome of the DPCR5 Competition Test process.

2.43 The modifications rename and renumber the current condition and replace the current wording with a new condition. The new condition retains much of the current condition, but includes the following changes:

- removal of the mechanism for licensees to apply for margin regulation to be lifted in relevant market segments that pass a legal requirements test and competition test
- removal of Appendix 2 of the licence condition that requires licensees to provide an independent audit report verifying that systems and processes are in place to comply with connections regulations and distributed generation connection standards.

2.44 The revised condition also adds a mechanism for the Authority to direct the level of margin that the licensee may charge for connection activities in market segments where the Authority has not determined that effective competition has been established.

2.45 The title has been updated as a consequence of the changes.

2.46 The effect of this condition is to enable the licensee to recover an unregulated margin on contestable connection activities in Relevant Market Segments that had passed the legal requirements and competition tests by 31 December 2013. The amendment enables the Authority to determine the level of margin that the licensee may recover on contestable connection activities in relevant market segments that had not passed the legal requirements and competition tests by 31 December 2013.

CRC 2L. Revenue adjustments in respect of performance failures

Type of change: Amendment

Current number: CRC 12 – Appendix 3.

Current name: Licensee’s Connection Activities: Margins and the development of competition. Appendix 3 – Revenue adjustments in respect of performance failures.

2.47 The modifications replaces CRC 12 – Appendix 3 with a new condition, CRC 2L. The reason for the modification is to introduce a separate licence condition for revenue adjustments in respect of connection performance failures. Our changes also simplify the current licence condition structure.

2.48 In the modified condition we have:

- updated the licence condition and the revenue exposure to reflect that RIIO-ED1 is an eight-year-long price control
- simplified the formula.

2.49 The effect of this condition is to continue current arrangements that place an overall cap on licensees’ liabilities under the connection Guaranteed Standards of Performance scheme, with payments beyond this level being funded through distribution use-of-system charges.

CRC 2M. Adjustment of licensee’s revenues for the residual distribution losses incentive

Type of change: Amendment

Current number: CRC 7

Current name: Adjustment of licensee’s revenues to reflect distribution losses performance

2.50 We are proposing to modify this condition for the following reasons. The residual losses incentive from the DPCR4 price control period (the PPL term) was originally due to be recovered during DPCR5 through licence condition CRC 7. Owing to volatility of data used to measure losses in 2009-10, we are still in the process of closing out the losses mechanism for DPCR4 and have yet to direct the PPL term. On 25 April 2013, we issued a letter stating that the earliest year for which we will be directing recovery of the PPL term is likely to be 2015-16, the first year of RIIO-ED1. That letter also made clear that we will direct the period for recovery taking account of the date on which the direction is made.¹⁰

Therefore we propose to include a licence condition in the RIIO-ED1 licence to update the current CRC 7 condition. This will allow recovery of the PPL term during RIIO-ED1, giving effect to the policy intent that we have already communicated on this issue.

Chapter 3

CRC 3A. Legacy price control adjustments

Type of change: New condition – all licensees including WPD licensees

2.51 The reason for introducing this new condition is update licensees’ revenue allowances, during RIIO-ED1, for the close-out of specific schemes that were introduced under the DPCR5. The adjustments are needed because complete data on which to close out the DPCR5 schemes is not available when setting licensees’ final determinations.

2.52 The effect of this condition, along with the associated Part 3 of the Handbook, is to provide a process through which licensees’ allowed revenue can be adjusted through the annual iteration of the PCFM.

¹⁰ Timing of recovery of the close out values of the losses incentive mechanism of the Fourth Distribution Price Control Review (DPCR4) - <https://www.ofgem.gov.uk/publications-and-updates/timing-recovery-close-out-values-losses-incentive-mechanism-fourth-distribution-price-control-review-dpcr4>

2.53 This condition was developed as part of the slow-track licence development process and applies to all licensees including WPD licensees.

CRC 3B. Determination of PCFM Variable Values relating to actual Totex expenditure for Totex Incentive Mechanism Adjustments

Type of change: New condition

2.54 The reason for introducing this new condition is to provide for the determination and direction of revised PCFM Variable Values relating to the licensee's actual levels of Totex expenditure. Under the Annual Iteration Process for the Price Control Financial Model, the licensee's actual level of Totex expenditure is compared to its allowed Totex expenditure levels. Through application of the Totex Incentive Strength rate for the licensee and the Totex Capitalisation Rate, an appropriate adjustment to allowed revenue is calculated to reflect any overspend or underspend under the sharing factor mechanism.

2.55 The effect of introducing this condition is to enable an adjustment to be made to the licensee's allowed revenue to reflect any over or under spend when compared to corresponding allowed Totex expenditure levels.

CRC 3C. Specified financial adjustments

Type of change: New condition

2.56 The purpose of this new condition is to provide for the determination and direction of revised PCFM Variables Values that will be used in the Annual Iteration Process for the ED1 Price Control Financial Model to make appropriate adjustments to:

- revenue allowances relating to Pension Scheme Established Deficit costs
- revenue allowances in respect of tax trigger events
- revenue allowances relating to the licensees' gearing levels and corporate debt interest costs
- the licensees' allowed percentage cost of corporate debt.

2.57 The effect of this condition is to provide for adjustments to be made to licensee's allowed revenue in respect of these factors.

CRC 3D. The Innovation Roll-out Mechanism

Type of change: New condition

2.58 The purpose of this condition is to establish the Innovation Roll-out Mechanism. This implements our policy set out in the Strategy Decision that licensees would be able to apply for funding for the roll-out of proven innovative solutions with low carbon and/or environmental customer benefits where the licensee cannot fund the roll-out under the current price control settlement.

2.59 The effect of this condition is to allow licensees to give notice to the Authority to seek an adjustment to their allowed revenue to fund the costs of rolling out a proven innovation. This condition explains:

- the criteria licensees must address when giving notice to the Authority under this condition
- the minimum value for which the licensee is permitted to make a notice for a relevant adjustment (an adjustment to licensee’s allowed revenue which allows it to roll out an innovation)
- when the licensee may give notice
- the process the Authority must follow when reaching its decision regarding a notice
- how any relevant adjustments are incorporated into the licensees’ allowed revenue.

CRC 3E. Smart Meter Roll-out Costs

Type of change: New condition.

2.60 The reason for introducing this condition is to provide for a mechanism for recovering the efficient costs of smart meter roll-out costs.

2.61 The effect of the condition is to establish a volume driver mechanism which:

- sets the opening values of the licensee’s allowed expenditure
- establishes the basis upon which that base level of smart meter roll-out costs can be varied to take account of the actual volume of smart meter installations when the licensees have been required to intervene
- provides a mechanism for feeding this adjustment into the Price Control Financial Model
- sets out the reporting requirements for this mechanism.

CRC 3F. Arrangements for the recovery of uncertain costs

Type of change: Amendment - all licensees except Scottish and Southern Energy Power Distribution: Scottish Hydro Electric Power Distribution (SSEH)

Current number: CRC 18 (excluding Part E)

Current name: Arrangements for the recovery of uncertain costs

2.62 The reason and effect of this condition is to allow for the recovery, of certain additional costs that are considered uncertain at the time of setting the price control, including a new provision for the recovery of planned rail electrification costs not recoverable from third parties.

2.63 We have updated the areas of cost covered by this mechanism from those in the current condition. The details of the cost areas that are included are in the Strategy decision. We have also updated how adjustments to revenues as a result of the application of this condition will impact allowed revenues. Adjustments now impact revenue through a change in MOD which is the output of the annual iteration of the Price Control Financial Model (PCFM).

CRC 3G. Revising the allowed level of Load Related Expenditure

Type of change: Amendment

Current number: CRC 18 (Part E)

Current name: Arrangements for the recovery of uncertain costs

2.64 Part E of CRC 18 enables the licensee to apply for allowances for following categories of efficiently incurred load-related costs to be amended in certain circumstances and at specified application windows:

- general reinforcement
- connections
- fault-level reinforcement
- transmission connection points.

2.65 We have modified Part E of CRC 18 so that it aligns with our Strategy Decision by:

- uncoupling it from CRC 18 into a discrete condition
- broadening the scope of cost areas that are eligible to be reopened during the price control period in line with the Strategy Decision
- clarifying the applicable application windows, and
- where the Authority considers that the information provided by the licensee is inadequate, a mechanism within a prescribed period to enable the Authority to “stop the clock” on the period within which it must assess a reopener request until the deficiency is remedied.

CRC 3H. Allowed expenditure on improving services to Worst Served Customers

Type of change: New condition

2.66 The reason for this condition is to facilitate improvements in services to more frequently interrupted customers.

2.67 The effect of this condition is to allocate capped funding to each licensee for the RIIO-ED1 period, through a formula which provides a value for the Price Control Financial Model and to improve services to worst served customers on its network. The condition also requires the licensee to ensure that the amount of expenditure on improving services to any one worst served customer does not in total exceed a cap per customer.

CRC 3I. Not used

Type of change: New condition

2.68 The reason for introducing this condition is to provide the licensee with clarity that that this condition is not used in the pack of their CRCs.

2.69 The introduction of this condition has no effect on any party

CRC 3J. Allowed expenditure on Visual Amenity Projects

Type of change: New condition

2.70 The reason for this new condition is to provide a capped allowance to the licensee for the replacement of overhead electricity cables with undergrounding in designated areas, where such a scheme is supported by relevant stakeholders, in accordance with our Strategy Decision.

2.71 The effect of this condition is to enable additions to be made to MOD by direction of the Authority through the operation of a PCFM Variable Value under the circumstances referred to above.

Chapter 4

CRC 4A. Governance of ED1 Price Control Financial Instruments

Type of change: New condition

2.72 The reason for introducing this new condition is to incorporate the ED1 Price Control Financial Handbook and the ED1 Price Control Financial Model (PCFM) into the licence and establish the change control framework for both of them. Both the ED1 Price Control Financial Model and the ED1 Price Control Financial Handbook form part of CRC 4A and may only be modified by the Authority in accordance with the provisions set out in this condition.

2.73 Given both the ED1 Price Control Financial Model and the ED1 Price Control Financial Handbook are part of the licence and are specific to each licensee, WPD have them both implemented with the RIIO-ED1 licence as part of the fast-track licence statutory consultation and modification notice. For slow-track companies, they will be implemented as part of the slow-track licence statutory consultation and modification notice.

2.74 The effect of introducing this condition is to establish and provide governance for the ED1 Price Control Financial Handbook and the ED1 Price Control Financial Model, both essential for the Annual Iteration Process that will update the licensee's base revenues during the price control period.

2.75 The latest versions of WPD's ED1 Price Control Financial Handbook and PCFM have been published as part of this document – see Schedules 2B and 2C.

CRC 4B. Annual Iteration Process for the ED1 Price Control Financial Model

Type of change: New condition

2.76 The purpose and effect of this new condition is to:

- set out the steps to be taken for the annual iteration process of the ED1 Price Control Financial Model
- set out the procedure for directing the value of the terms MODt to the licensee.

Chapter 5

CRC 5A. The Network Innovation Competition

Type of change: New condition

2.77 The reason for introducing this condition is to reflect the Network Innovation Competition (NIC) policy outlined in the Strategy Decision. Under the NIC the licensee can bid for funding through a competitive process for innovative projects which have low carbon and/or environmental benefits.

2.78 The effect of the condition is to enable the licensee to fund eligible NIC projects. This includes:

- establishing the NIC funding and the funding return mechanism, which outline the circumstances under which the licensee will receive funding and the circumstances under which the licensee must return money
- establishing that the regulation, governance and administration of the NIC will be detailed in the NIC governance document, the document associated to the licence
- establishing that the licensee must comply with the NIC governance document as if it formed part of the licence
- establishing the procedures for issuing and revising the NIC governance document.

CRC 5B. Restriction of charges for the provision of Legacy Metering Equipment

Type of change: Amendment

Current number: CRC 6

Current name: Restriction of charges for the provision of Legacy Metering Equipment

2.79 The purpose of this condition is to establish the restrictions on charges for the provision of legacy metering equipment and to set out the obligations on the licensee. Consequential modifications are required to this condition to ensure that it is capable of continuing to operate as currently, notwithstanding changes elsewhere in the licence.

2.80 The effects of these modifications are:

- to modify the definition of inflation (RPIit) so that it is included within this condition, rather than in another licence condition that will employ a different definition of inflation
- to change the condition number and referencing within this condition, to ensure that it remains operational over the RIIO-ED1 price control period.

CRC 5C. Directly Remunerated Services

Type of change: Amendment

Current number: CRC 15

Current name: Services treated as Excluded Services

2.81 The purpose of this condition is to set out the services provided by the licensee that are to be treated as directly remunerated services. It also specifies the basis on which charges can be levied for directly remunerated services. The changes are:

- to change the name of the condition from Services treated as Excluded Services, which reflected the fact that revenue does not count towards allowed distribution network revenue, to directly remunerated services. This name is a better description because it refers to the main characteristic of the service – ie that it is paid for by the party commissioning the service rather than by use of system charge payers
- to make clear in Part A that any returned royalty income through the Network Innovation Competition is not revenue from a directly remunerated service
- to add two new Directly Remunerated Service categories:
 - DRS 7-smart meter roll-out rechargeable services that are provided under the provisions of the Service Level Agreement that is appended to the DCUSA and fall outside the definition of smart meter roll-out costs
 - DRS8-value added services: to incentivise DNOs to allow relevant assets to be used for data and communications infrastructure and for other commercial opportunities and to provide for interaction with the Totex Incentive Mechanism, so that net gains from providing such services are shared with electricity consumers.
- to renumber the miscellaneous category as DRS9.

2.82 The effects of the changes are:

- to ensure that the condition remains applicable for the RIIO-ED1 price control period and to improve its clarity, in particular:
 - to provide for smart meter roll-out rechargeable services to be provided on a cost-recovery basis
 - to introduce a mechanism by which the licensee and electricity consumers can share gains from the appropriate exploitation of network assets, for example under commercial arrangements for the installation of third-party data or communications equipment.

CRC 5D. Assessment of Network Asset Secondary Deliverables

Type of change: New condition.

2.83 This condition establishes the licensee’s Network Asset Secondary Deliverables for the price control period as set out in the Network Assets Workbook.

The Network Assets Workbook forms part of the licence and will be subject to change only through a licence modification, or through a specific process for rebasing the workbook where the Common Network Asset Indices Methodology is amended. Since the Network Assets Workbook for WPD is part of this licence condition it has been published as part of this notice – see Schedule 2D: Network Assets Workbook.

2.84 The condition also:

- sets out the basis on which the Authority intends to make its assessment of the licensee’s delivery of the Network Asset Secondary Deliverables
- specifies the incentive that will be provided in respect of justified over-delivery, and penalty for under-delivery that is not justified, of the Network Asset Secondary Deliverables.

2.85 The effect of this condition is to require the licensee to provide a report to the Authority that is consistent with the Common Network Asset Indices Methodology. The report will allow the Authority to assess the licensee’s performance in delivering the Network Asset Secondary Deliverables for the purpose of determining what, if any, adjustments should be made to the licensee’s allowed revenue in the next price control period.

CRC 5E. Charging outside the Distribution Services Area

Type of change: Amendment

Current number: CRC 16

Current name: Charging outside the Distribution Services Area

2.86 We have amended the wording in Part A of the condition to avoid any possible ambiguity in the current licence condition around how the licensee must set out of area charges. The amendments make clear that the licensee must set out of area charges such that the standing charge, unit rate and any other component of the charge taken together do not exceed the use of system charges to equivalent domestic customers.

2.87 We have removed and update the provisions in parts B and C of this condition relating to the disapplication of out of area charges. The provisions are being moved to CRC 5K (Disapplication).

2.88 The effect of these amendments is to clarify current policy.

CRC 5F. Services for managing Theft of Electricity from the Distribution System

Type of change: New condition

2.89 The reason is to ensure that consumers share some benefit in income arising from actions taken by licensees in respect of Relevant Theft of Electricity.

2.90 The effect of this condition is to apply the Efficiency Incentive Rate sharing factor to such income by applying an amount equal to it as a negative adjustment to totex allowed revenue.

CRC 5G. Net to gross adjustment for Load Related Expenditure

Type of change: New condition

2.91 The reason for this condition is to provide a means for ensuring that the licensee is not able to recover twice for the provision of connections and reinforcement services to its network, through both distribution use of system (DUoS) charges and through connection charges.

2.92 The effect of this condition is to set out the baseline volumes of connections and baseline percentage of gross load-related expenditure that the licensee is expected to deliver during the price control period. The condition establishes a framework under which the Authority may make adjustments to the licensee's base revenue in the next price control period (RIIO-ED2), where any of the actual percentage of gross load-related expenditure funded through specific customer-funded reinforcement during the price control period exceeds the relevant net-to-gross threshold.

CRC 5H: Not used

Type of change: New condition

2.93 The reason for introducing this condition is to provide the licensee with clarity that that this condition is not used in the pack of their CRCs.

2.94 The introduction of this condition has no effect on any party.

CRC 5I: Not used

Type of change: New condition

2.95 The reason for introducing this condition is to provide the licensee with clarity that that this condition is not used in the pack of their CRCs.

2.96 The introduction of this condition has no effect on any party.

CRC 5J: Not used

Type of change: New condition

2.97 The reason for introducing this condition is to provide the licensee with clarity that that this condition is not used in the pack of their CRCs.

2.98 The introduction of this condition has no effect on any party.

CRC 5K. Disapplication

Type of change: Amendment

Current number: CRC 19

Current name: Duration of the Charge Restriction Conditions

2.99 The reason for the modification is to align the disapplication condition with the licence modification appeals process set out in the Act, which has replaced the former licence modification reference process.

2.100 The effect of our amendments is to ensure that the condition remains up-to-date with the appeals process set out in the Act and also to improve the clarity of how the disapplication provisions are set out in the licence by bringing the provisions previously set out CRC 16 and CRC 19 into a single licence condition.

Removal of existing CRCs

2.101 The following current CRCs will be removed from the licence.

CRC 9. Adjustment of licensee's revenues to reflect performance in relation to Transmission Connection Point Charges

Type of change: Complete removal from the licence

2.102 The purpose of this current condition is to provide an incentive on certain elements of transmission connection point charges that the DNOs could influence through talking to the transmission operator.

2.103 The reason for the removal of this condition is that under the RIIO-ED1 price control settlement, these charges are included as part of the companies' opening base revenue allowance, and incentivised through the Totex Incentive Mechanism. Therefore a separate incentive condition is no longer required for these costs.

2.104 The effect of this deletion is to remove a provision that is covered elsewhere in RIIO-ED1 price control settlement.

CRC 10. Adjustment of licensee's revenues to reflect innovation funding performance

Type of change: Complete removal from the licence

2.105 The Strategy Decision set out that we would establish a Network Innovation Allowance (NIA) and that the innovation funding incentive would be incorporated into the NIA. The NIA is reflected in the new condition CRC 2H (Network Innovation Allowance).

2.106 The effect of this modification is to remove CRC 10 from the licence.

CRC 11. Adjustment of licensee's revenues to reflect performance in relation to Distributed Generation

Type of change: Complete removal from the licence

2.107 We have removed this licence condition to reflect the decision to discontinue the Distributed Generation (DG) Incentive scheme. The justification for the decision to discontinue the DG Incentive is set out in the Strategy Decision for the RIIO-ED1 electricity distribution price control: outputs, incentives and innovation supplementary annex, chapter 3.¹¹

¹¹Strategy decision for the RIIO-ED1 electricity distribution price control Outputs, incentives and innovation - https://www.ofgem.gov.uk/sites/default/files/docs/2013/02/riioed1decoutputsincentives_0.pdf



2.108 The effect of this modification is to remove an out-of-date licence condition.

CRC 17. Assistance for high-cost distribution areas

Type of change: Complete removal from the licence - all licensees except SSEH

2.109 We propose to remove this condition as it is not applicable to any licensee other than SSEH.

2.110 The effect of this change is to remove a redundant condition from the DNOs licences.

3. Associated documents to the CRCs

Chapter Summary

An outline of the purpose and content of the associated documents that are governed by the CRCs.

Question 1: Do you have any comments on the associated documents that we propose to create and their content?

What is an associated document?

3.1. Associated documents are ancillary to the licence. They provide guidance or instructions to the DNOs on specific policy areas. They vary in content but all give the licensee more information on specific schemes in the licence, including:

- the process that will be followed to derive an adjustment in allowed revenue
- governance arrangements or guidance for participating in a scheme
- details on what, and how, information should be reported by the licensee.

3.2. The process for issuing and modifying associated documents is set out in the licence condition that covers the related scheme. We have proposed the same process for issuing and modifying all associated documents.

3.3. For both issuing and modifying associated documents the Authority issues a direction. Before issuing the direction there will be a 28-day consultation by notice, setting out the reasons and effects of proposed changes. The Authority will then consider responses and give reasons for the final decision as part of the direction.

3.4. Associated documents may contain both non-binding guidance and instructions which the licensee must comply with as if they were part of the licence. Where possible, these elements will be differentiated within the documents.

3.5. As part of the fast-track process, we outlined the purpose and content of the associated documents that we propose to create for RIIO-ED1.¹² This chapter provides an update on the development of these documents.

¹² RIIO-ED1: Informal consultation on fast-track licence drafting – Charge Restriction Conditions (Part 1) - <https://www.ofgem.gov.uk/publications-and-updates/riio-ed1-informal-consultation-fast-track-licence-drafting-%E2%80%93-charge-restriction-conditions-part-1>

RIIO-ED1 associated documents

Stakeholder Engagement Incentive Guidance

3.6. The draft licence condition CRC 2C (Broad Measure of Customer Service) establishes the Stakeholder Engagement Incentive Guidance, and its scope and governance arrangements. The purpose of this guidance is to provide detailed information on how the Stakeholder Engagement Incentive works.

3.7. At the last ENA Customer and Social Issues Working Group (CSIWG), we outlined our proposed approach, which is to incorporate social objectives into the Stakeholder Engagement Incentive. DNOs will provide their feedback at the next ENA CSIWG, on 29 September 2014.

3.8. We intend to consult on the RIIO-ED1 Stakeholder Engagement Incentive Guidance at the end of October 2014. Our revised guidance will explain how the incentive will include our assessment of social objectives.

Incentive on Connections Engagement Guidance

3.9. The draft licence condition CRC 2E (Incentive on Connections Engagement) establishes the Incentive on Connection Engagement Guidance, and its scope and governance arrangements. The purpose of this document is to:

- outline the criteria
- state how the Incentive on Connections Engagement submissions will be assessed
- explain how the Authority will determine the applicable penalty.

3.10. The document will:

- reiterate the objectives of the ICE
- outline the scope of the scheme
- confirm the submission process for licensees (eg the submission format and the submission dates)
- state the assessment process (eg the objective criteria, how we will assess submission and how we will determine whether to apply a penalty).

3.11. We published a draft Incentive on Connections Engagement Guidance and trialled the proposed arrangements in summer 2014 (based on distributed generation market segments only).

3.12. As part of the trial arrangements, we consulted with stakeholders about:

- how well the DNOs engaged with connection stakeholders during 2013-14, and

- the DNOs' proposed plans to improve their connections service during 2014-15.

3.13. We intend to discuss the trial, and how well it has worked, with the RIIO-ED1 Connections Working Group. We plan to consult on the RIIO-ED1 Incentive on Connections Engagement Guidance at the end of October 2014.

Losses Discretionary Reward Guidance

3.14. The draft licence condition CRC 2G (Losses Discretionary Reward) establishes the Losses Discretionary Reward Guidance Document (LDRGD), and its scope and governance arrangements. The Losses Discretionary Reward is a payment to licensees whose activities meet the criteria associated with managing electricity distribution losses. These criteria are explained in the LDRGD.

3.15. The rules and criteria of the LDRGD are still to be developed. In our strategy decision we explain that the reward will be made in three tranches over RIIO-ED1. The strategy decision also contains our initial thinking on the criteria for measuring DNOs' performance.¹³ These could include categories such as:

- companies' understanding of their losses performance and preparation for a measureable losses incentive in RIIO-ED2
- effectiveness of actions taken to reduce losses
- engagement with customers on managing losses
- innovative approaches to reducing losses
- performance against the Distribution Losses Strategy
- sharing of best practice with other companies.

Participating DNOs will need to submit evidence against the criteria.

3.16. The LDRGD will also show the processes for submission and assessment. It will list the deadlines for submission and the timing of the milestones leading to the final decision on each tranche. The LDRGD apply to all participating DNOs.

1.7. The LDRGD will be developed with stakeholders and issued in a timely manner after the publication of the final determinations for the slow-track companies.

Network Innovation Allowance (NIA) Governance Document

3.17. The draft licence condition CRC 2H (The Network Innovation Allowance) establishes the NIA Governance Document, and its scope and governance arrangements. This guidance describes the regulation, governance and administration of the Electricity NIA, which is available to all licensees as part of the price control allowance.

¹³ See March Strategy Decision – Outputs, Incentives and Innovation, 5.11 – 5.14, pages 43-44
https://www.ofgem.gov.uk/sites/default/files/docs/2013/02/riioed1decoutputsincentives_0.pdf

3.18. The document is currently in force for electricity transmission licensees. It contains:¹⁴

- the NIA eligibility requirements
- the project registration process
- the NIA knowledge dissemination requirements.

3.19. We propose to amend the electricity transmission NIA Governance Document to refer to electricity distribution where it currently only refers to electricity transmission. We plan to also review the governance arrangements once they have been in place for electricity transmission licensees for two years. Any changes following this review would also affect electricity distributors who will share the same NIA Governance Document.

3.20. Any changes will be consulted on before being implemented.

3.21. The document is currently in force for electricity transmission licensees. Early in 2015, we will consult on a new version of it that incorporates DNOs and IDNOs.

Low Carbon Networks (LCN) Fund Governance Document

3.22. The draft licence condition CRC 2J (Low Carbon Networks Fund) establishes the LCN Fund Governance Document, and its scope and governance arrangements. The purpose of the governance document is to set out the regulation, governance and administration of the LCN Fund, which is available to all licensees.

3.23. The document is currently in force for DNOs.¹⁵ The current document will need to be amended. We intend to remove those parts of the document pertaining to the First Tier funding and the operation of the Second Tier competition process. Those requirements associated with the Funding Directions, will be retained to allow funds for the final competition to be transferred as required; as well as allow royalties and ineligible expenditure to be returned to customers in the event this is needed. All requirements to successfully implement ongoing Second Tier Projects will be retained. Any changes will be consulted on before being implemented.

3.24. In summary we expect the updated document to include:

- detail of the Discretionary Reward Scheme
- the Second Tier Funding Mechanism
- the requirements that ongoing Second Tier projects must comply with

¹⁴ Electricity Network Innovation Allowance Governance Document - <https://www.ofgem.gov.uk/publications-and-updates/electricity-network-innovation-allowance-governance-document>

¹⁵ Low Carbon Networks Fund Governance Document - <https://www.ofgem.gov.uk/ofgem-publications/45703/low-carbon-networks-fund-governance-document-version-6.pdf>

- default arrangements for intellectual property rights.

3.25. We will consult on a new version early in 2015. It will be in place for the start of RIIO-ED1.

Network Innovation Competition (NIC) Governance Document

3.26. The draft licence condition CRC 5A (The Network Innovation Competition) establishes the electricity NIC Governance Document, and its scope and governance arrangements. The purpose of the NIC Governance Document is to set out the regulation, governance and administration of the Electricity NIC - an annual competition designed to help network companies operate more innovatively.

3.27. The document is currently in force for electricity transmission licensees. It contains:¹⁶

- the NIC eligibility requirements
- the NIC evaluation requirements
- the NIC process
- the requirements that licensees implementing projects must comply with
- the NIC knowledge dissemination requirements.

3.28. The document will need to be amended so that it also refers to electricity distribution. We also plan to review the governance arrangements once they have been in place for electricity transmission licensees for two years. Any changes following this review would also affect electricity distributors who will share the same NIC Governance Document.

3.29. We will consult on a new version early in 2015. It will be in place for the start of RIIO-ED1.

¹⁶ Electricity Network Innovation Allowance Governance Document - <https://www.ofgem.gov.uk/publications-and-updates/electricity-network-innovation-Competition-governance-document>

4. ED1 Price Control Financial Handbook

Chapter summary

An outline of the purpose and content of Part 1 and Part 2 of the ED1 Price Control Financial Handbook governed by CRC 4A.

Question 1: Do you have any comments on the draft of Part 1 and Part 2 of the ED1 Price Control Financial Handbook included in supplementary annex 2?

4.1. The draft licence condition CRC 4A (Governance of ED1 Price Control Financial Instruments) establishes the ED1 Price Control Financial Handbook ('the handbook') and its associated governance arrangements.

4.2. The purpose of the handbook is to provide licensees, and other interested parties, with the process steps and methodologies that will be followed during RIIO-ED1. These will cover annual remodelling of licensees' base revenue allowances through the 'Annual Iteration Process' of the Price Control Financial Model

4.3. The ED1 Price Control Financial Handbook is part of the licence and is specific to each licensee. It therefore needs to be implemented through licence statutory consultation and modification notice.

4.4. The handbook is split into three parts:

Part 1: introductory chapters

Part 2: the methodologies that will be followed during RIIO-ED1 to update revenue allowances for RIIO-ED1 policy-related schemes. These are the schemes found in CRC 3B to CRC 3J of the proposed licences for the slow-track DNOs.

Part 3: the methodologies that will be followed during RIIO-ED1 to update revenue allowance to close out DPCR5 schemes. These DPCR5 schemes will be closed out under new licence condition CRC 3A (Legacy price control adjustments) and Part 3 of the handbook. Part 3 and CRC 3A will apply to all licensees, including WPD's licensees. Chapter 5 explains our approach to closing out DPCR5 schemes and why we have made changes to the methodologies originally set out in DPCR5 Final Proposals.¹⁷

¹⁷ Electricity Distribution Price Control Review Final Proposals - <https://www.ofgem.gov.uk/publications-and-updates/electricity-distribution-price-control-review-final-proposals>

5. Close out of DPCR5 schemes

Chapter summary

An outline of our proposed approach to closing out DPCR5 schemes during RIIO-ED1

Question 1: Do you agree with our approach to closing out DPCR5 schemes during RIIO-ED1?

Introduction

5.1 There are a number of DPCR5 schemes that need to be closed out at the inception of, or during, the RIIO-ED1 price control period. This is in order to reflect the DNOs' position at the end of DPCR5 (ie 31 March 2015). Closing out these schemes will typically involve adjusting DNOs' allowed revenue in RIIO-ED1.

5.2 In the DPCR5 Final Proposals,¹⁸ we described how many of these schemes would be closed out. However, the introduction of the Annual Iteration Process under RIIO allows us to close out these schemes using reported data received once DPCR5 has ended.

5.3 We are therefore consulting on changing the DPCR5 policy in order to use the Annual Iteration Process to close out these schemes.

5.4 We have described, and are consulting on, our proposed process and timing for closing out these schemes in the ED1 Price Control Financial Model Handbook.

DPCR5 schemes and our proposed approach to closing them out

5.5 Table 2 shows the DPCR5 schemes that must be closed out during the RIIO-ED1 price control period and the original close-out approach set out in DPCR5.

5.6 There are two reasons for our proposal to deviate from the process that was set out at DPCR5.

- **Reason 1**

For some DPCR5 schemes, there is no need to wait to make the close-out adjustment at DPCR7 (RIIO-ED2), as stated in DPCR5 Final Proposals. This is because the Annual Iteration Process allows us to make them sooner.

¹⁸ Electricity Distribution Price Control Review Final Proposals - <https://www.ofgem.gov.uk/publications-and-updates/electricity-distribution-price-control-review-final-proposals>

▪ **Reason 2**

Where we had stated in DPCR5 that we will use forecast data to close out a particular scheme, we now propose to wait for the full set of actual data to be reported during RIIO-ED1 before closing out each specific scheme. In the DPCR5 Final Proposals we described the RPI-X approach where we would not change allowed revenues once the price control had begun. The introduction of the Annual Iteration Process as part of RIIO means that, unlike previous price control settlements, we can make these adjustments in a timely fashion during the RIIO-ED1 price control period. We think it is in the interests of both consumers and DNOs to wait to use actual data to close out DPCR5 schemes.

Table 2: DPCR5 schemes requiring close out during RIIO-ED1

DPCR5 schemes	Close out approach in DPCR5¹⁹
RAV Rolling Incentive	N/A
DUoS Bad debt	N/A
Distributed Generation (DG) incentive	Base close out on forecast (years not specified)
Enhanced Physical Site Security (CNI) and Black Start	Use forecast data for 2014-15 with, ex post true up in DPCR7 if material.
High-value projects reopener	Use forecast data for 2014-15.
Load-related reopener	Use forecast data for 2014-15.
Network output measures	Assess on a basis of 4 years actual and forecast. If penalty is applied, may be subject to true up with last year of actual data.
Rising and lateral mains reopener	Use forecast data for 2014-15. Not subject to true up but there is a potential adjustment if more costs are recovered from consumers or third parties than anticipated at DPCR5.
Undergrounding	Base on forecast (years not specified). Recover any overfunding in DPCR6 if materially different.
Workforce renewals	N/A
Worst served customers	Base on forecast (years not specified). Recover any overfunding in DPCR6 if

¹⁹ As set out in DPCR5 Final Proposals - <https://www.ofgem.gov.uk/publications-and-updates/electricity-distribution-price-control-review-final-proposals>

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	materially different.
Deferred rev exp tax pool opening balance adjustment	N/A
General tax pool opening balance adjustment	N/A
Pension ongoing service costs true-up	N/A
Pension Protection (PPF) levy true-up	N/A
Special tax pool opening balance adjustment	N/A
DPCR5 FP: use forecast data for 2014-15ax claw back	N/A
Traffic Management Act (TMA) permitting schemes reopener	Use forecast data for 2014-15. Not subject to true up. Any logging costs are subject to an ex post efficiency review.
Volume driver on high-volume low-cost connections	Use forecast data for 2014-15. Ex post true-up in DPCR7 if materially different.

Appendices

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2	Outline of the new structure of the CRCs in the RIIO-ED1 licence	45
3	Feedback questionnaire	47

Appendix 1 – consultation response and questions

1.1. We would like to hear your views on any of the issues set out in this document.

1.2. We especially welcome responses to the specific questions at the beginning of each chapter. These are replicated below.

1.3. Responses should be received by 24 October 2014 and should be sent to clothilde.cantegreil@ofgem.gov.uk

1.4. Unless marked confidential, all responses will be published in our library and on our website, www.ofgem.gov.uk. You may request that your response be kept confidential. We will respect this request, unless the law requires us to disclose anything, for example under the Freedom of Information Act 2000 or the Environmental Information Regulations 2004.

1.5. If you'd like your response to remain confidential, clearly mark the document to that effect and include the reasons for confidentiality. Put any confidential material in the appendices to your response.

1.6. We intend to publish our decision on the draft CRCs after considering the responses to this consultation. Any questions should initially be directed to:

- Clothilde Cantegreil
- 0207 901 3195
- clothilde.cantegreil@ofgem.gov.uk

Chapter two

- **Question 1:** Do you have any views on the proposed changes to the CRCs? The draft licence conditions are found in supplementary annex 1.
- **Question 2:** Do you have any views on the reasons and effects for the licence changes proposed in this consultation?

Chapter three

- **Question 1:** Do you have any comments on the associated documents that we propose to create and their content?

Chapter four

- **Question 1:** Do you have any comments on the draft of Part 1 and Part 2 of the ED1 Price Control Financial Handbook included in this consultation?

Chapter five

- **Question 1:** Do you agree with our approach to closing out DPCR5 schemes during RIIO-ED1?

Appendix 2 – outline of the CRC structure for RIIO-ED1 licence

RIIO-ED1 Condition number and name		Current DPCR5 licence condition	Associated document?	Draft Condition in Supplementary Annex 1?
Chapter 1: Interpretation of Part 4				
1A	Overview of Part 4	CRC 1	No	No
1B	Interpretation of Part 4	CRC 2	No	No
Chapter 2: Electricity Distribution Revenue Restriction				
2A	Restrictions of Allowed Distribution Network Revenue	CRC 3, 5 and 14	No	No
2B	Calculation of Allowed Pass-through Items	CRC 4	No	No
2C	Broad measure of customer service	CRC 8	Yes	No
2D	Adjustment of licensee’s revenues to reflect interruptions related quality of service performance	CRC 8	No	No
2E	Incentive on Connections Engagement	New	Yes	No
2F	Time to Connect Incentive	New	No	No
2G	The Losses Discretionary Reward	New	Yes	No
2H	The Network Innovation Allowance	New	Yes	No
2I	Not Used	New	No	No
2J	Low Carbon Networks Fund	CRC 13	Yes	No
2K	Margins on Licensee’s Connection Activities	CRC 12	No	No
2L	Revenue adjustments in respect of performance failures	CRC 12	No	No
2M	Adjustment of licensee’s revenues for the residual distribution losses incentive	CRC 7	No	Yes
Chapter 3: Annual Iteration Process - Adjustments to the Revenue Restriction				
3A	Legacy price control adjustments	New	No	Yes
3B	Determination of PCFM Variable Values relating to actual Totex expenditure for Totex Incentive Mechanism Adjustments	New	No	No
3C	Specified financial adjustments	New	No	No
3D	The Innovation Roll-out Mechanism	New	No	No
3E	Smart Meter Roll-out Costs	New	No	No
3F	Arrangements for the recovery of uncertain costs	CRC 18	No	No

RIIO-ED1: Informal consultation on slow-track licence drafting – Charge Restriction Conditions

RIIO-ED1 Condition number and name		Current DPCR5 licence condition	Associated document?	Draft Condition in Supplementary Annex 1?
3G	Revising the allowed level of Load Related Expenditure	CRC 18	No	No
3H	Allowed expenditure on improving services to Worst Served Customers	New	No	No
3I	Not Used	New	No	No
3J	Allowed Expenditure on Visual Amenity Projects	New	No	No
Chapter 4: Price Control Financial Instruments				
4A	Governance of ED1 Price Control Financial Instruments	New	No	No
4B	Annual Iteration Process for the ED1 Price Control Financial Model	New	No	No
Chapter 5: Other Revenue Restriction Related Conditions				
5A	The Networks Innovation Competition	New	Yes	No
5B	Restriction of charges for the provision of Legacy Metering Equipment	CRC 6	No	No
5C	Directly Remunerated Services	CRC 15	No	No
5D	Assessment of Network Asset Secondary Deliverables	New	No	No
5E	Charging outside the Distribution Services Area	CRC 16	No	No
5F	Services for managing Theft of Electricity from the Distribution System	New	No	Yes
5G	Net to gross adjustment for load related expenditure	New	No	No
5H	Not used	New	No	No
5I	Not used	New	No	No
5J	No used	New	No	No
5K	Disapplication	CRC 19	No	No
Proposed Removal from Current Licence				
9	Adjustment of licensee's revenues to reflect performance in relation to Transmission Connection Point Charges	Removal	No	NA
10	Adjustment of licensee's revenues to reflect innovation funding performance	Removal	No	NA
11	Adjustment of licensee's revenues to reflect performance in relation to Distribution Generation	Removal	No	NA
17	Assistance for high-cost distribution areas	Removal	No	NA

Appendix 3 – feedback questionnaire

1.1. Consultation is at the heart of good policy development. We are keen to consider any comments or complaints about the way this consultation has been conducted. We would be keen to get your answers to the following questions:

1. Do you have any comments about the overall process which was adopted for this consultation?
2. Do you have any comments about the overall tone and content of the report?
3. Was the report easy to read and understand? Could it have been better written?
4. To what extent did the report's conclusions provide a balanced view?
5. To what extent did the report make reasoned recommendations for improvement?

1.2. Please add any further comments and send your response to:

Andrew MacFaul
Consultation Co-ordinator
Ofgem
9 Millbank
London
SW1P 3GE
andrew.macfaul@ofgem.gov.uk