Transmission and Distribution Policy
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Consultation on a proposal to increase significantly the notification period for changes to distribution use of system charges

EDF Energy is one of the UK's largest energy companies with activities throughout the energy chain. Our interests include nuclear, coal and gas-fired electricity generation, renewables, and energy supply to end users. We have over five million electricity and gas customer accounts in the UK, including residential and business users.

EDF Energy has been campaigning for predictability of network charge for some time. We believe that at a time when many customers are struggling to pay their bills, it is essential that all costs are minimised. In the case of distribution use of system changes, we strongly believe that the cost of managing the risk arising from charging volatility is better placed with the distribution companies, rather than by suppliers/customers. In reaching this view, we note that the marginal cost of funds for many vulnerable customers (e.g. from pay-day lenders) is likely to be much higher than those available to a DNO.

In 2012 we commissioned Cambridge Economic Policy Associates (CEPA) to produce a report[1] on the volatility of such charges and the ability of relevant industry parties to manage the associated risk. The report concluded that the benefits of predictability (in terms of competition impacts and reduced supply costs) could exceed any costs that might be incurred by the DNOs from the options evaluated and that, based on this analysis, the emphasis should be on providing a 15 or 27 months notice period of future DUoS charges between and within price controls.

While the consultation on measures to mitigate network charging volatility arising from the price control settlement added additional measures that will help both customers and suppliers, further steps are needed. In particular, extending the notification period to 15 months for DUoS charges is necessary to address the risk associated with (often significant) annual movements in charges (see our attached analysis below). This will

[1] https://www.ofgem.gov.uk/ofgem-publications/50525/cepa-edf-volatility-reportfinal-260912.pdf

reduce the cost to the customer and allow suppliers to manage DUoS charges without including a risk premium for distribution charging volatility in their pricing (especially for small suppliers that do not have a diverse portfolio).

Certain types of larger customers, especially those under the EHV Distribution Charging Methodology (EDCM), experience significant volatility that neither they, nor suppliers, are able to mitigate. Consequently when the volatility is too high customers are being exposed to the whole risk of changes to these charges.

Our detailed responses are set out in the attachment to this letter. Should you wish to discuss any of the issues raised in our response or have any queries, please contact Simon Vicary on 02031262167, or myself.

I confirm that this letter and its attachment may be published on Ofgem's website.

Yours sincerely,

Paul Delamare
Head of Downstream Policy and Regulation

Attachment

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EDF Energy's response to your questions

- **Do you agree with the working group's view that DCP178 would result in these benefits and costs?**

There would be significant benefit to customers from having longer notice periods for DUoS charges. The volatility which is inherent with the Price Control methodology means it is difficult for DNOs to predict what their charges will be in future periods with the only the base allowed revenues numbers being certain. All other components can and do vary by significant amounts.

With DCP178 the DNOs would be delayed in receiving some of their allowed revenues but they would still recover the amounts set out by the regulator. Suppliers and customers face the complete opposite problem in that it is impossible to forecast DUoS charges accurately and any error in the forecast means there is a risk of over paying or under recovering of what is a regulated cost.

Analysis shows that for a domestic customer this can vary significantly from one DNO to another. Looking at forecasting April 2014 charges a year in advance shows that the risk can be as large as £21or as little as £2 depending where you are based in the country.

We understand that some parties feel that by increasing the notification period for charges there is additional risk for the DNOs but the risk is only down to a delay in cash flow whereas suppliers are exposed to any changes in charges not forecast. This is particularly important for small suppliers who do not have a broad portfolio of customer types which can help to spread some of this risk.

- **Are there any other benefits and costs that you think would result from DCP178?**

Small suppliers will benefit from greater certainty enabling them to compete more effectively in the market.

- **For suppliers and customers, can you provide supporting evidence for the benefits identified by respondents to the working group's consultations?**

We have attached our analysis based on a domestic customer and the changes to charges over a period of time. The analysis demonstrates that the forecast price movements provided by the DNO (in their respective DCP066 reports) are an unreliable guide to the

eventual outturn, and that there is a significant degree of volatility in the charges themselves (despite the years considered not being transition years between one price control period and another).

- **Do you think the proposed notice period would cause any issues with implementing any changes to charges which may be required due to developments in the operation of the network?**

Changes to the charging methodology already take a considerable time to implement as the process is often complicated and time-consuming. We have been encouraging the industry to provide longer notice periods for any changes that impact charges. It is unreasonable to make significant changes to customer's charges without a sufficient notice period.

With DCP178 customers will have ample time to understand and respond to the impact of any changes to their tariffs.

- **Do the benefits of certainty outweigh any costs or effects of delay?**

From a customer perspective the benefits will certainly outweigh the effects of any delay. With 15 months notice suppliers will be able to offer fixed contracts to a much wider range of customers than currently by knowing that the risk to the business has been removed in the short-term.

- **Can you give examples over the next five years of likely changes to distribution charges that are critical to deriving benefits but which would be delayed unduly if DCP178 was approved?**

We are not aware of any changes to DUoS charges that would have significant material impact if they were further delayed through the implementation of DCP178.

We note that the future developments set out in Ofgem's consultation are, in the main, long term issues that will develop relatively slowly. For example, we would not expect the pace of heat/transport electrification, local/renewable generation, smart meter/grid and European developments to be quick enough to be materially impacted by a 15 month notice period for charging changes. In any case, if there were such changes, it is only fair that suppliers and customers have adequate warning of them, and that DNOs are best placed to understand and finance the cost of any such volatility.

We note that Ofgem also refers to the cost of deferring implementation of changes to specific elements of smart meter or smart grid development. However, it is important to realise that it is only changing charges that would be delayed, not the actual activities of a DNO in these areas.

EDF Energy
September 2014

Comparison of forecast and actual changes in DUOS prices between 2013/14 and 2014/15	Eastern Power Networks UKPN	East Midlands WPD	London Power Networks UKPN	Scottish Power Manweb SPD	West Midlands WPD	Northern NPG	Elctricity North West ENW	Scottish Hydro SSE	Scottish Power SPD	Eastern Power Networks UKPN	Southern SSE	South Wales WPD	South West WPD	Yorkshire NPG	Average	Minimum Variance	Maximum Variance
Annual bill for Domestic Unrestricted 3,200kWh in 2013/14	£73.50	£77.25	£79.09	£124.88	£87.45	£95.08	£104.87	£153.62	£92.16	£88.02	£87.30	£122.29	£122.48	£83.59	£99.40		
Forecast April 2014 based on DCP066 reports published in February 2013																	
- percentage change to 2013/14 prices	17.2%	18.4%	12.2%	14.2%	9.0%	13.4%	7.6%	7.0%	-3.0%	13.6%	9.0%	6.4%	9.5%	11.2%	10.4%		
- forecast of 2014/15 prices	£86.14	£91.48	£88.74	£142.61	£95.31	£107.82	£112.82	£164.37	£89.39	£99.99	£95.16	£130.12	£134.11	£92.95	£109.36		
- difference between forecast and actual 2014/15 prices (£)	£4.72	£13.60	£15.43	£2.35	£11.63	£0.84	£8.52	£20.79	-£2.06	£10.68	£7.69	£9.15	£12.76	£3.34	£8.53	-£2.06	£20.79
Forecast April 2014 based on DCP066 reports published in May 2013																	
- percentage change to 2013/14 prices	16.0%	15.0%	9.7%	13.6%	9.4%	8.8%	8.6%	7.0%	-1.2%	12.9%	8.9%	6.5%	8.7%	10.6%	9.6%		
- forecast of 2014/15 prices	£85.29	£88.84	£86.75	£141.82	£95.64	£103.43	£113.92	£164.42	£91.06	£99.34	£95.03	£130.20	£133.15	£92.43	£108.67		
- difference between forecast and actual 2014/15 prices	£3.86	£10.96	£13.44	£1.56	£11.97	-£3.54	£9.62	£20.84	-£0.39	£10.03	£7.56	£9.23	£11.79	£2.82	£7.84	-£3.54	£20.84
Forecast April 2014 based on DCP066 reports published in August 2013																	
- percentage change to 2013/14 prices	15.2%	13.8%	8.6%	14.5%	7.6%	7.5%	6.3%	10.3%	-1.0%	12.8%	9.0%	2.4%	6.3%	8.8%	8.7%		
- forecast of 2014/15 prices	£84.67	£87.89	£85.89	£143.01	£94.13	£102.20	£111.45	£169.46	£91.21	£99.28	£95.13	£125.25	£130.20	£90.97	£107.91		
- difference between forecast and actual 2014/15 prices	£3.25	£10.02	£12.58	£2.74	£10.45	-£4.78	£7.16	£25.88	-£0.24	£9.97	£7.66	£4.28	£8.84	£1.36	£7.08	-£4.78	£25.88
Forecast April 2014 based on DCP066 reports published in November 2013																	
- percentage change to 2013/14 prices	12.4%	10.8%	7.9%	13.4%	5.1%	14.0%	5.7%	2.7%	-2.5%	11.1%	4.5%	2.2%	3.1%	9.8%	7.2%		
- forecast of 2014/15 prices	£82.61	£85.55	£85.34	£141.59	£91.94	£108.36	£110.88	£157.77	£89.87	£97.80	£91.19	£124.92	£126.28	£91.77	£106.13		
- difference between forecast and actual 2014/15 prices	£1.19	£7.68	£12.04	£1.33	£8.26	£1.39	£6.59	£14.19	-£1.58	£8.49	£3.72	£3.95	£4.92	£2.16	£5.31	-£1.58	£14.19
April 2014/15 Final published prices	£81.43	£77.88	£73.31	£140.26	£83.68	£106.97	£104.30	£143.58	£91.45	£89.31	£87.47	£120.97	£121.36	£89.61	£100.83		
- percentage change to 2013/14 prices	10.8%	0.8%	-7.3%	12.3%	-4.3%	12.5%	-0.5%	-6.5%	-0.8%	1.5%	0.2%	-1.1%	-0.9%	7.2%	1.7%		
Risk that customer could have faced if priced in February 2013 for a 2 year contract																	
- percentage difference	6.4%	17.6%	19.5%	1.9%	13.3%	0.9%	8.1%	13.5%	-2.2%	12.1%	8.8%	7.5%	10.4%	4.0%	8.7%		
- price difference (£)	£4.72	£13.60	£15.43	£2.35	£11.63	£0.84	£8.52	£20.79	-£2.06	£10.68	£7.69	£9.15	£12.76	£3.34	£8.53	-£2.06	£20.79