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for energy consumers

Independent Distribution Network
Operators and other interested
parties

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Date: 4 April 2018

Supplier of Last Resort – derogation to Independent Distribution Network Operators in respect of Co-Operative Energy Limited’s Last Resort Supply Payment claim

This letter covers a direction on all electricity Independent Distribution Network Operators (IDNOs) with a Use of System charging methodology approved by the Authority.¹

Background

We published our decision on 7 February 2018 to grant a request from all Distribution Network Operators (DNOs) for a derogation from their charging methodology and the notice period required due to a Last Resort Supply Payment (LRSP) claim by Co-Operative Energy.² DNOs have subsequently published amended Use of System charges effective from 1 April 2018.

Standard licence condition (SLC) 13.1 of the electricity distribution licence states the licensee must have in force at all times, and comply with, a Use of System charging methodology approved by the Authority. Amended Standard Condition BA2.3 of each IDNO’s licence also requires them to set Use of System Charges in relation to Domestic Customers that do not exceed the Use of System Charges to equivalent Domestic Customers in a given DNO region.

In order to comply with their licence requirements, IDNOs, who have had a charging methodology approved by Authority, have set out that their charging methodology is to replicate the Use of System charges of the relevant DNO.

Reasons for a derogation

The approach taken by DNOs to recover the LRSP amount will result in an increase in charges for residential customers connected to DNO networks, but not for those customers on IDNO networks or for non-residential customers. We said in our decision that we do not expect IDNOs to increase charges to their customers, as they have not incurred any additional costs. Furthermore, SLC38 which provides the mechanism for recovering an LRSP claim and returning it to the claimant, does not apply to IDNOs.

¹ References to the “Authority”, “Ofgem”, “we” and “our” are used interchangeably in this document. The Authority refers to GEMA, the Gas and Electricity Markets Authority. The Office of Gas and Electricity Markets (Ofgem) supports GEMA in its day to day work.

² <https://www.ofgem.gov.uk/publications-and-updates/decision-grant-all-dnos-derogations-charging-years-201819-and-201920-due-last-resort-supply-payment-claim>

This however creates a conflict with the IDNOs' approved Use of System charging methodology (that is, to replicate the charges of the DNO in whose region they are operating). We therefore consider that a derogation is needed from SLC 13.1 so that IDNOs are not required to comply with their charging methodology insofar as it is necessary to avoid the effects described above. For clarity, we thus expect each IDNO's Use of System charges to be no higher than the relevant DNO, less any amount attributable to recovery of any LRSP costs.

Our decision and next steps

We have considered this issue in accordance with our principal objective and statutory duties and decided that a derogation from SLC 13.1 of the electricity distribution licence is necessary in this case.

Concerning the overall Supplier of Last Resort process, our view remains that all consumers benefit from these protections and that, in principle, the cost should be spread across all consumers. This has not been possible in this case due to the circumstances and timings associated with the claim, and the current licence drafting. We will work with DNOs, IDNOs and other interested stakeholders to understand what changes are needed for the future.

If you have any questions regarding this letter, please contact David McCrone (david.mccrone@ofgem.gov.uk) in the first instance.

Yours sincerely

Chris Brown
Head of Core and Emerging Policy
Signed for and on behalf of the Authority

Direction made by the Gas and Electricity Markets Authority

To:

1. ESP Electricity Ltd;
2. Independent Power Networks Ltd;
3. The Electricity Network Company Ltd;
4. Energy Assets Power Networks Ltd;
5. G2 Energy IDNO Ltd;
6. Harlaxton Energy Networks Ltd;
7. Leep Electricity Networks Ltd;
8. UK Power Distribution Ltd;
9. Fulcrum Electricity Assets Ltd;
10. Energetics Electricity Ltd.

WHEREAS:

- A. Each of the companies to whom this Direction is addressed (each an "IDNO") holds a licence granted, or treated as granted, pursuant to section 6(1)(c) of the Electricity Act 1989 (the "Distribution Licence") and has a charging methodology approved under Standard Licence Conditions ("SLC") 13.1 of such licence as described further below.
- B. GEMA issued a Direction ("LRSP Direction")³ to all Distribution Services Providers⁴ on 6 February 2018, in response to a valid claim for a Last Resort Supply Payment by Co-Operative Energy Limited. The LRSP Direction was not addressed to IDNOs. As a result, use of system charges for domestic customers on each Distribution Services Provider's network will increase.
- C. SLC 13.1 of the Distribution Licence requires all holders of a Distribution Licence to comply with the Charging Methodology as set out in SLC 13 and as approved by GEMA. SLC 13.1 gives GEMA the power to grant a derogation from the obligation to comply with the Charging Methodology.
- D. Amended Standard Condition BA2.3 of each IDNO's Distribution Licence requires IDNOs to set Use of System Charges in relation to Domestic Customers that do not exceed the Use of System Charges to equivalent Domestic Customers in the Distribution Services Area⁵.
- E. In order to ensure compliance with the requirement described in recital D above, the approved Charging Methodology of each of the IDNOs replicates the equivalent use of system charges of the Distribution Services Provider of each Distribution Services Area.
- F. The effect of complying with a Charging Methodology on the terms described in recital E where each Distribution Service Provider has increased charges as described in B would be to increase charges to users of the IDNO's network where there has been no corresponding change to the costs borne by the IDNO.
- G. GEMA therefore considers it appropriate to make the Direction set out below, for the reasons set out in the accompanying letter dated 4 April 2018, which constitutes

³ https://www.ofgem.gov.uk/system/files/docs/2018/02/coop_solr_derogation_letter_0.pdf

⁴ As defined in Condition 1 of the Distribution Licence.

⁵ As defined in Condition 1 of the Distribution Licence.

GEMA's notice of reasons pursuant to the Electricity Act 1989.

NOW THEREFORE:-

1. GEMA hereby directs pursuant to SLC 13.1 that each IDNO:

is not required to comply with its Charging Methodology approved pursuant to SLC 13, only insofar as it is necessary to avoid the effect described in recital F.

2. The direction shall have effect from the date stated below.

Dated: 4 April 2018

Chris Brown
Head of Core and Emerging Policy
Signed for and on behalf of the Authority