

28 March 2018

Office of Gas and Electricity Markets
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Sent by email only to: alena.fielding@ofgem.gov.uk

Dear Alena

Response to: Notice of statutory consultation on a proposal to modify Standard Condition 12 of all electricity distribution licences

This response is provided in response to Ofgem's statutory consultation on proposed modifications to Standard Condition 12 of the electricity distribution licence. This follows the implementation of the "*The Electricity (Connection Offer Expenses) Regulations 2018*" ("the Regulations") which come into effect on the 6 April 2018. We understand that:

- the proposed modification to standard licence condition 12.7 removes from electricity distributors the obligation to enter into an agreement for connection until an applicant has paid connection offer expenses.
- whilst the right to recover connection offer expenses comes into effect on the 6 April, until the proposed modification to licence condition 12 comes into effect, electricity distributors cannot use the non-payment of connection offer expenses as a reason for not entering into an agreement for connection.

Effect of proposed modification to standard condition 12 of the electricity distribution licence and the implementation of the Regulations

The drafting of paragraph 2(2) of the Regulations states that the distributor can only

*"...require the applicant to pay expenses relating to the application that **have been reasonably incurred**..."¹.*

The use of the words "*...have been reasonably incurred...*" is very specific. We believe the only interpretation that can be applied to this is that the electricity distributor must first incur the expenses before they can require them to be paid; i.e. the assessment and design must have been undertaken before payment can be requested. To comply with the regulations, we think the electricity distributor must:

- first, prior to incurring the expenses, provide a notice to the applicant setting out that such expenses need to be paid as set out in paragraph 2(4) of the Regulations, and
- second, after the expenses have been incurred, provide a notice in accordance with the provisions set out in paragraph 2(3).

¹ Emphasis added

We do not think that licence condition drafting or DNO charging statements can 'overrule' the Regulations in this respect.

The proposed drafting of licence condition 12.7 (c) gives the relevant licensee the right to refuse "...to offer to enter into an agreement for connection... if the requester has not paid the relevant connection offer expenses required by the licensee in accordance with...[the Regulations]". Given that the assessment and design work must have been undertaken for the relevant licensee to request payment for expenses, electricity distributors should be obliged to offer to enter into an agreement for connection *immediately* following payment of the relevant connection offer expenses.

Connection Charging Methodology and Charging Statement

We think it is in the interests of all classes of connection customer that a common approach across all electricity distributors is adopted. Introduction and implementation of connection offer expenses should be carried out in a coordinated way. We think the arrangements for connection offer expenses must be set out in the common connection charging methodology, with the charges set out in electricity distributor's charging statements.

This is consistent with Government's response to BEIS' consultation² where they stated:

"The methodology for charging applicants will be a matter to be determined in the regulatory framework and DNO charging documents, overseen by Ofgem".

And that

"There are governance arrangements in place that require Ofgem approval of each DNO's Connection Charging Methodology (CCM)¹¹ and Connection Charging Statement (CCS)¹ DNOs will therefore have to co-ordinate the introduction of new arrangements to agree and then propose a common approach to their CCS for Ofgem to approve".

As a minimum we think the charging methodologies and statements must:

- Set out the basis on how connection offer expenses are calculated. (Paragraph 2.(2) of the regulations appears to set out the framework of charges that should be included in the charging methodology and charging statement. This is also consistent with the requirements of paragraph 2(3) (b) of the Regulations).
- Set out how charges differentiate between:
 - (i) work where the assessment and design has been undertaken by an accredited third party;
 - (ii) work where only design and assessment up to the point of connection is undertaken (i.e. the network extension is designed by an accredited third party or is owned and operated by another distributor);
 - (iii) costs for re-quotations when no material changes are required; or
 - (iv) work undertaken in whole by the electricity distributor.

- Set out how connection offer expenses will be recovered where work is common for multiple requests for connection at the same site. Expenses should not be recovered several times over.
- Set out how connection offer expenses will be apportioned where works undertaken will also benefit wider customer base (e.g. reinforcement).
- Set out how connection offer expenses fall within the scope of the Electricity Connection Charge Regulations and what happens where a first comer pays the assessment and design fees, but a second comer subsequently progresses the connection.

We are concerned that electricity distributors may not adopt a common approach, methodology or form of charging statement to set out the basis of such charges. In addition, we understand that some distributors may be looking to apply charges as set out in their charging statement but that neither the methodology for the basis of such charges, nor the form of such charges has been approved (or in the case of the methodology does not exist).

For example, in respect of Northern Power Grid, their charging methodology does not set out the methodology setting out how the amounts in their charging statement are determined; nor can we find any reference on Ofgem's website for the approval of changes to the form of charging statement to allow such charges to be levied. (We recognise that Ofgem does not approve the charges themselves).

We recognise the concerns of electricity distributors (DNOs) on the recovery of the costs of servicing connection applications in an efficient manner. In principle we are not against the introduction of assessment and design fees. We note that prior to 2008, not all DNOs charged upfront A&D fees. We understand their largest area of concern was with connection requests for generation, which by their nature can be speculative since ownership of generation sites has not been secured at the time of the request. However, for new housing developments, the fact that houses will be built is usually not speculative (even though they may be built out over a longer time period. Although the developer for a site may change over the life of a site, the electricity requirements for the site will not change, and the original work on assessing and designing works required on the existing distribution system to service the site will remain unchanged (in the majority of cases).

The connections market has seen competition develop significantly over the last five years which has provided the developer customers choice and competition in terms of delivery and costs. This has in large part been because of interventions by Ofgem. It would be unfortunate if the implementation of arrangements for connection offer expenses inhibited the competition in the connections market – one of Ofgem's success stories.

When we complained to Ofgem in 2008 on the legitimacy of levying Assessment and Design fees, we had significant concerns about:

- the arbitrary and excessive way such charges had been levied, (by one DNO in particular);
- that such charges were recovered several times over where there were multiple applications for a site. (Whilst we recognise the design of the network extension may (but not always) differ between developers, there will be much common work in the

assessment of the existing of works required on the existing distribution system – particularly where applications are for competing ICPs for the same development).

We have always been clear that in parallel with the introduction of arrangements giving electricity distributors the right to recover connection off expenses, there must be an effective and realistic alternative whereby an accredited third party can undertake the assessment and design of a large part of the works, and thereby avoid the costs.

In the development of the Competition in Connections Code of Practice we were keen to see arrangements introduced whereby suitably accredited agents could access DNO systems and undertake their own assessment and design. My understanding is that work in this area has only progressed slowly with current arrangements being ineffective and not offering a cost or time effective alternative to accredited third parties. We are concerned that the introduction of connection offer expenses will have the unintended consequence of acting as a further disincentive to DNOs facilitating effective arrangements for self-assessment – so that DNOs can retain the work and recover expenses.

We believe that transparency in setting out how such charges will be calculated and applied is essential in maintain a level playing field. We would welcome the opportunity to come and talk to Ofgem to explain our concerns in more detail.

Yours sincerely

Michael Harding
Regulation Director