

All stakeholders

Email: RetailPriceRegulation@ofgem.gov.uk

Date: 25 November 2020

Dear Stakeholders,

### **Consultation on changes to 'Annex 3 – Methodology for determining the Network Cost Allowance' of SLC 28AD**

The purpose of this letter is to consult stakeholders on how we propose to determine the Network Cost Allowance within the default tariff cap ("cap") from the sixth charge restriction period (April 2021 – September 2021) onward. Data inputs previously used to determine the network cost allowance have changed in structure or availability. This requires us to identify alternative data sources and amend the structure and format of the 'Network cost allowance methodology elec' and 'Network cost allowance methodology gas' spreadsheet models ("models") forming Annex 3 of SLC 28AD<sup>1,2</sup> to accurately reflect the changes. We are also required to update the 'Supplementary workbook to Annexes 2, 3 and 4 – Demand and losses' ("supplementary workbook") as part of the amendments.

A summary of the changes in data inputs can be found below.

- Following the change to the Distribution Connection and Use of System Agreement (DCUSA) under Distribution Change Proposal (DCP) 268,<sup>3</sup> the electricity Distribution Use of System (DUoS) charges set for April 2021 are based on a three-unit rate tariff. This consultation sets out how we propose to determine DUoS costs at the Benchmark Annual Consumption Levels<sup>4</sup> from this date. We also set out how we propose to calculate the share of demand in the supplementary workbook as part of the updated methodology.
- The existing gas target volumes of National Transmission System (NTS) capacity used to weight exit zones in Annex 3 are published up to March 2021. This consultation considers an alternative data source to use after this date.

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<sup>1</sup> Licence Conditions on Ofgem website:

<https://www.ofgem.gov.uk/licences-industry-codes-and-standards/licences/licence-conditions>

<sup>2</sup> Annex 3 includes the 'Network cost allowance methodology - elec' and the 'Network cost allowance methodology - gas'.

<sup>3</sup> DCP268 - DUoS Charging Using HH Settlement Data - <https://www.ofgem.gov.uk/publications-and-updates/dcp268-duos-charging-using-hh-settlement-data>

<sup>4</sup> The 'Benchmark Annual Consumption Levels' are the levels of annual consumption at which the network cost allowance is calculated. For electricity, these are nil kWh, 3,100 kWh for single-register metering arrangements and 4,200 kWh for multi-register metering arrangements.

- Following the introduction of Uniform Network Code (UNC) 678A<sup>5</sup> in October 2020, the existing terminology and reference to 'SO exit charge' and 'TO exit charge' in Annex 3 no longer accurately reflects the gas transmission charging regime that is in place. This consultation sets out how we propose to account for gas transmission exit commodity charges in Annex 3 from April 2021.

In this letter we have set out our proposed approach, which we think represents the best option for determining the network cost allowance. We have provided detailed information on the proposed changes to the models and the supplementary workbook in the Annex of this letter. We have also published the draft revised models and supplementary workbook alongside this letter.

We want to ensure transparency with stakeholders and provide this opportunity to comment ahead of setting the default tariff cap for the next charge restriction period, in February 2021.

## **Background**

The cap includes a network cost allowance to ensure that suppliers are able to recover costs that are incurred through gas and electricity network charges. The network cost allowance is set out and calculated in the models. This allowance accounts for electricity distribution, transmission and balancing costs as well as gas distribution and transmission costs.

We calculate network costs for each six-monthly cap period, using information on charges from the network companies' charging statements with assumptions about demand and losses. We estimate the costs to a supplier for different metering arrangements and charge restriction regions.

## **Electricity DUoS costs**

Electricity DUoS charges are published by the distribution network companies in their annual charging statements.<sup>6</sup> Currently, unrestricted and two-rate domestic customers are charged a fixed charge and either a single or a two rate unit charge, respectively. This is reflected in the electricity network cost allowance model in Annex 3.

On 8 April 2019, Ofgem approved the modification to the DCUSA DCP268 to align settlement for both demand and generation for each half hourly settlement period. DCP268 will change the DUoS charge tariff structure so that all domestic customers are charged a fixed charge and a three-rate, time of use Red/Amber/Green (RAG) unit charge, from April 2021. The RAG unit rate charges are based on consumption within each time band over a given day. To calculate the DUoS charges at the Benchmark Annual Consumption Levels<sup>7</sup> from April 2021, we need to allocate consumption to the RAG time bands for single-rate and multi-register customers.

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<sup>5</sup> Amendments to Gas Transmission Charging Regime: Decision and Final Impact Assessment (UNC678/A/B/C/D/E/F/G/H/I/J) - <https://www.ofgem.gov.uk/publications-and-updates/amendments-gas-transmission-charging-regime-decision-and-final-impact-assessment-unc678abcdefghij>

<sup>6</sup> Example of a Distribution Network Operator's Charging Statement (Use of System charges, Annex 1): <http://www.westernpower.co.uk/About-us/Use-of-system-charges/Use-of-System-Charges.aspx>

<sup>7</sup> We are not required to update the methodology to calculate DUoS charges at the nil kWh Benchmark Annual Consumption Level as the fixed charge structure (p / day) remains unchanged.

## Proposal

To allocate consumption to RAG time bands, we propose to determine the share of demand that takes place in half-hourly settlement periods in the supplementary workbook, using Elexon's demand data. The most recent demand year's data will be used to calculate the share of demand for each cap period. The half-hourly share of demand in each settlement period will be split between Monday – Friday (including bank holidays) and Saturday – Sunday. For single-rate and multi-register metering arrangements, we will calculate the share of demand for Profile Class 1 and Profile Class 2, respectively. We have published the proposed updates to the supplementary workbook alongside this consultation, setting out these calculations.

Our proposed changes to the electricity network cost allowance model take the half-hourly demand data from the supplementary workbook and use it to allocate consumption to the RAG time bands in each charge restriction region. For each metering arrangement and region, a weighted unit charge is calculated as the sum of the products of the RAG unit rates and the share of demand in the RAG time bands. This charge is multiplied by the Benchmark Annual Consumption Levels and combined with the annual fixed charge.

### **Exit zone weightings for ECN charges**

The gas network cost allowance model in Annex 3 includes the Distribution Network target volume of NTS Exit (Flat) Capacity as published in the gas transporter licence special conditions.<sup>8</sup> The target volume of capacity by exit zone is used to weight capacity markets for individual exit zones when calculating Exit Capacity NTS (ECN) charges at the regional, Local Distribution Zone (LDZ) level. The values in the licence are published up to 2020/21. We are required to find a new source of weights after this year to weight exit zones when calculating future ECN charges at LDZ level.

## Proposal

From 2021/22, we propose to use the Baseline Obligation values published in National Grid Gas's long term summary reports<sup>9</sup> to weight the exit zones in the gas network cost allowance model. The Baseline Obligation is the volume of Enduring NTS Exit (Flat) Capacity made available, defined in the licence by each exit point. These values are higher than the previous source as they reflect the volumes National Grid Gas are required to make available compared to what is expected to be booked. However, the offtake volumes reflect a similar distribution between exit zones within an LDZ so we consider them suitable for use as a weighting factor.

For the sixth charge restriction period, we propose to add the Baseline Obligation volumes to the existing NTS capacity by exit zone table and update the source in the gas network cost allowance model. The existing table would also be updated to include Cambridge, Lauderhill and Crawley Down offtakes and rename 'Moss-side' to 'Burnhervie'.<sup>10</sup> Weighted ECN charges at LDZ level would continue to be calculated using the current methodology.

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<sup>8</sup> Gas Transporter Licence Special Conditions, Chapter 1, Appendix 2 (p40):

<https://epr.ofgem.gov.uk/Content/Documents/Wales%20and%20West%20Utilities%20Limited%20-%20Special%20conditions%20consolidated%20-%20Current%20Version.pdf>

<sup>9</sup> National Grid Gas's Exit Capacity Publications, Allocation & Release Obligation LT Summary Report and Baseline Capacity Statement: <http://mip-prd-web.azurewebsites.net/ExitCapacityPublication/Index>

<sup>10</sup> Direction to modify National Grid Gas's gas transporter licence: <https://www.ofgem.gov.uk/ofgem-publications/53273/exit-points-covering-letter.pdf>

We do not expect the proposed weightings to have a significant impact on the gas transmission cost allowance.

We propose to update the weightings annually as part of the February update. We would use the Baseline Obligation volumes for the beginning of the next cap period, as published in the most recent summary report.

### **Gas transmission exit commodity costs**

Gas transportation charges are published every six months in the Notice of Gas Transmission Transportation Charges<sup>11</sup> by National Grid Gas. The System Operator (SO) and Transportation Operator (TO) exit commodity charges that were previously published in this notice reflected the gas transmission commodity costs in the gas network cost allowance model. These charges are referenced in the model as 'SO exit charge' and 'TO exit charge'.

On 28 May 2020, Ofgem approved the modification proposal UNC678A: 'Amendments to Gas Charging Regime (Postage Stamp)' to be implemented from 1 October 2020. As a result of the amendments in UNC678A, the gas transmission commodity charges no longer exist in their previous form. In August 2020, we published a letter<sup>12</sup> to inform stakeholders of a change to input values used in the network cost allowance for the fifth cap period, given the introduction of UNC678A. Due to the timing of when the transportation charges were published, we were unable to amend the model structure before publishing the cap level for the fifth cap period.

#### *Proposal*

We propose to change the structure of the gas network cost allowance model to better align with the gas transmission commodity charges from the sixth cap period onward. The structure of the gas transmission cost allowance for the fifth cap period will not change as a result of our proposal.

We propose to remove the input provided under 'SO exit charge' from the gas network cost allowance model and add the 'General Non-Transmission Services Exit Charge' as a new input. Under UNC678A, this charge replaced the 'SO exit charge' and did not change substantially apart from re-naming. We will use the same methodology to calculate 'General Non-Transmission Services Exit Charges' at the Benchmark Annual Consumption Levels.

We also propose to remove the input for 'TO exit charge' from the sixth cap period onward. The costs of the new NTS capacity charges for the exit capacity booked at Distribution Network offtakes will be levied on Gas Distribution Network Operators, and passed through to suppliers via ECN charges. We expect the NTS Exit Capacity Charges from October 2020 to be accounted for in the April 2021 ECN charges.

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<sup>11</sup> Notice of Gas Transmission Charges October 2020 (National Grid Gas): <https://www.nationalgrid.com/uk/gas-transmission/document/132056/download>

<sup>12</sup> Gas networks input availability letter (7 August 2020): <https://www.ofgem.gov.uk/publications-and-updates/default-tariff-cap-gas-networks-input-availability>

## **Next steps and consultation responses**

We welcome views on the proposed changes set out in this letter. We ask stakeholders to send any comments to [RetailPriceRegulation@ofgem.gov.uk](mailto:RetailPriceRegulation@ofgem.gov.uk) by **close of business on 4 January 2021**.

Yours faithfully,

Anna Rossington  
Deputy Director, Retail Price Protection

## **Annex 1: Detailed model modifications**

Updated cells are highlighted in the models and supplementary workbook published alongside this letter. A summary of the modifications can be found below.

### **Electricity DUoS Charges**

#### Supplementary workbook to Annex 2, 3 and 4 – Demand and losses

##### 1b Demand weights

- Rows 30 – 81: Table added to calculate the share of demand in half-hourly settlement periods for each metering arrangement, Monday – Friday and on weekends.

#### Annex 3 – Network cost allowance methodology elec

##### 2b DUoS

- Cells B3:P3: Text updated.
- Cells W11:AB24 and W39:AB52: Calculation formulas updated to reference fixed DUoS charges in '3f DUoS charges (DCP268)'.
- Cells W25:AB38 and W53:AB66: Calculation formulas updated to sum the products of DUoS unit rates and time bands share of consumption in '3f DUoS charges (DCP268)'.

##### 3a Demand

- Rows 39 – 236: Time-series table added to input the share of demand from supplementary workbook.

##### 3d DUoS charges

- Cells B3:G3: Text updated.

##### 3e BSUoS charges

- Cells Q9:V9: Calculation formulas updated to reference fixed DUoS charges in '3f DUoS Charges (DCP268)'.

##### 3f DUoS charges (DCP268)

- New tab created.
- Rows 13 – 32: Time-series table added to input DUoS fixed charge.
- Rows 33 – 242: Time-series table added to input DUoS unit charges and calculate the share of demand for each metering arrangement, charge restriction region and time band (inputs in columns K – P and calculations in columns Q – V).

## **Exit zone weightings for ECN charges**

#### Annex 3 – Network cost allowance methodology gas

##### 3d NTS capacity by exit zone

- Cells B3:M3: Text updated.
- Rows 18, 90, 114: Rows added with input values for Cambridge, Crawley Down and Lauderhill offtakes.
- Cell C108: Name of 'Moss side' offtake updated to 'Burnhervie'.
- Cells K6:M6: Title of table 'Baseline Obligation of NTS Exit (Flat) Capacity (GWh/d)' added.
- Cells K8:K131: Volume of baseline capacity for April 2021 inputted from National Grid Gas's November 2020, long term summary report.

### 3e ECN charges

- Cells B3:U3: Text updated.
- Cells J9:J41: Indicative ECN charges for April 2021 inputted.<sup>13</sup>

## **Gas transmission exit commodity costs**

### Annex 3 – Network cost allowance methodology gas

#### 2b Gas transmission charges

- Cells B3:L3: Text updated.
- Rows 38 – 50: Calculations added for ‘Non-Transmission Services Exit Charge’.
- Cells U64:Z76: Calculations updated to reference ‘Non-Transmission Services Exit Charge’ in rows 38 – 50.

#### 3f NTS exit commodity charges

- Title of tab updated from ‘3f SO and TO exit charges’ to ‘3f NTS exit commodity charges’.
- Cells B2:H3: Text updated.
- Row 13: Row added for ‘Non-Transmission Services Exit Charge’.
- Cells C11:C13: Source link updated.
- Cell U13: Indicative ‘Non-Transmission Services Exit Charge’ for April 2021 added.<sup>14</sup>

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<sup>13</sup> Distribution Network’s Indicative Notices of Transportation Charges from 1 April 2021: <https://www.gasgovernance.co.uk/indic/2021>

<sup>14</sup> Notice of Indicative Gas Transmission Transportation Charges effective from 1 April 2021 (issued 31 October 2020): <https://www.nationalgrid.com/uk/gas-transmission/document/133521/download>