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for energy consumers

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Date: 27 March 2018

Dear Distribution Network Operators,

**Treatment of costs in respect of Co-Operative Energy Limited's Last Resort Supply Payment claim to be recovered through Electricity Distribution Use of System charges**

**Summary:**

We appointed Co-Operative Energy Limited ("CEL") as a Supplier of Last Resort with effect from 30 November 2016 to the customers of GB Energy Supply Limited after the latter ceased trading<sup>1</sup>. These Supplier of Last Resort Provisions allow CEL to recover certain additional costs as part of taking on this responsibility. These costs are recovered from electricity distribution and gas distribution companies who in turn pass these costs onto consumers through their charges.

This letter sets out how we expect the electricity distribution companies to recover these amounts and how they will be treated under our price control arrangements. These costs will be added to use of system charges to allow their recovery, but will be excluded from the "Regulated Distribution Network Revenues" term in the allowance so that the operation of the remainder of the price control is unaffected.

**Background:**

Standard Licence Condition ("SLC") 9, *Claims for Last Resort Supply Payment* ("LRSP") of the Gas and Electricity Supply Licences provides that a Supplier of Last Resort may make a claim for a LRSP to compensate for additional costs it has incurred in complying with a Last Resort Supply Direction, from relevant gas transporters and electricity distributors, where the Authority has given its consent to the amount claimed.

On 13 November 2017, CEL submitted notice of its intention to claim for a LRSP, which we approved in part on 19 January 2018. On 25 January 2018, CEL submitted its claim to the Gas Distribution Networks ("GDNs") and electricity Distribution Network Operators ("DNOs").

The DNOs are required, by paragraph 2 of SLC 38, *Treatment of payment claims for last-resort supply* of their Electricity Distribution Licences, to increase their Use of System Charges

<sup>1</sup> <https://www.ofgem.gov.uk/publications-and-updates/direction-appoint-cooperative-energy-gas-supplier-last-resort>  
<https://www.ofgem.gov.uk/publications-and-updates/direction-appoint-cooperative-energy-electricity-supplier-last-resort>

from 1 April 2018 to such an extent as they reasonably estimate is appropriate to ensure the consequential increase will equal the Specified Amount.

Paragraph 7 of SLC 38 provides that “in calculating the licensee’s Use of System revenue during any period for the purposes of any Charge Restriction Condition that may be applicable to the licensee under this licence, any increase or decrease in Use of System revenue attributable to the licensee’s compliance with this standard condition 38 must be treated as if it had not occurred”. This ensures that the operation of the remainder of the price control is not affected by the LRSP. In particular, that any increase in use of system charges is not treated as an over-recovery against allowed revenues, which would then be corrected through a future reduction in allowed revenues.

On 1 February 2018, Northern Powergrid wrote to the us on behalf of all DNOs to request a formal direction in respect of a derogation from SLC 13 of the Electricity Distribution licence and clause 19.1A of the Distribution Connection and Use of system Agreement (“DCUSA”) to be able to recover the costs associated with Co-operative Energy Limited’s Last Resort Supply Payment (“LRSP”).<sup>2</sup>

On 6 February 2018, we directed that DNOs are not required to comply with SLC 13.1 and clause 19.1A where non-compliance is necessary to allow the DNOs to be able to comply with their obligations under SLC 38, following the CEL LRSP claim.<sup>3</sup>

The remainder of this letter sets out our approach for the recovery of the CEL LRSP claim amounts, through an increase in Use of System charges that is to be excluded from the Regulated Distribution Network Revenues term in the Revenue Regulatory Reporting Pack. We have issued a separate direction to the GDNs directing the equivalent adjustment to be made through the Miscellaneous Pass-through term within the Gas Transporter Licence. We think this approach in gas provides additional transparency of the recovery of the LRSP. No such mechanism exists in the Electricity Distribution Licence, hence the different treatment set out below.

### **Regulatory treatment of LRSP amount:**

Charge Restriction Condition 2A (Restriction of Allowed Distribution Network Revenue) of the Electricity Distribution Licence contains term RDt, which represents the revenue earned by the DNO from Use of System Charges made for the provision of Distribution Services to customers in respect of a Regulatory Year.

In order for the electricity distribution companies to recover the LRSP amount, they must increase their Use of System charges. However, in order for the price control to operate as intended, this additional amount must be excluded from the reporting of the RDt term. This will ensure that it is not recognised as an over-recovery against allowed revenues and that no associated adjustment will be made in future years to return the over-recovery to consumers. To address this, the electricity distribution companies must exclude from their reporting of RDt, the amount collected from the consequential increase in Use of System revenues, reasonably made, in respect of the CEL LRSP Claim. This will effectively exclude the increased revenue from the 2018-19 Regulatory Reporting Pack submission process, and achieve the aims in SLC 38, paragraph 7.

### **Next Steps:**

We will audit the 2018-19 RDt term to ensure that the appropriate sums are recovered from consumers. The electricity distribution companies should make these adjustments as transparently as possible in their relevant communications on affected use of system of charges and also in their commentaries accompanying their affected regulatory submissions

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<sup>2</sup> <http://www.northernpowergrid.com/asset/0/document/4097.pdf>

<sup>3</sup> [https://www.ofgem.gov.uk/system/files/docs/2018/02/coop\\_solr\\_derogation\\_letter\\_0.pdf](https://www.ofgem.gov.uk/system/files/docs/2018/02/coop_solr_derogation_letter_0.pdf)

to us. The obligation to prepare and publish a statement on the above matters is outlined in SLC 38, paragraphs 9 and 10.

As per the CEL LRSP Claim letters sent to each DNO, the claim amounts are noted, below:

Electricity North West Limited	£620,480.33
Northern Powergrid (Northeast) Limited	£416,797.51
Northern Powergrid (Yorkshire) PLC	£598,469.44
Scottish Hydro Electric Power Distribution PLC	£199,713.20
Southern Electric Power Distribution PLC	£789,594.07
SP Distribution PLC	£521,870.57
SP Manweb PLC	£392,789.44
Eastern Power Networks PLC	£941,033.13
London Power Networks PLC	£606,718.51
South Eastern Power Networks PLC	£595,846.89
Western Power Distribution (East Midlands) PLC	£684,996.94
Western Power Distribution (South Wales) PLC	£293,753.74
Western Power Distribution (South West) PLC	£416,702.48
Western Power Distribution (West Midlands) PLC	£643,114.76

The position taken in this letter does not represent a legal precedent for future cases. We reserve the right to review any future claims arising, on a case by case basis.

If you have any queries, please contact Penny Harandy: [penny.harandy@ofgem.gov.uk](mailto:penny.harandy@ofgem.gov.uk) or on 020 7901 7098.

Yours sincerely,



**Geoffrey Randall**

**Associate Partner, RIIO Networks  
For and on behalf of the Authority**