

Mick Watson,
Head of Regulatory Finance Reporting, Systems & Networks
Ofgem
10 South Colonnade
Canary Wharf
London, E14 4PU

4 September 2020.

Sent by email to: regfinance@ofgem.gov.uk

Dear Mick,

Managing network charge bad debt – proposal enabling networks to recover potential bad debts arising from COVID-19 related deferred network charge payments and to introduce an enduring solution to bad debt recovery in general.

Thank you for the opportunity to submit our views on the above open letter. We consider the proposals for the enduring solution to bad debt recovery are sensible. However, we do not agree with the proposals for the recovery of COVID-19 related bad debt in 2021/22. Specifically, we object to the proposal to allow Electricity Distribution Network Operators (DNOs) to recover Network Charge Deferral Scheme (NCD) bad debt by changing 2021/22 DUoS tariffs.

- Changing 'Final' tariffs reduces market certainty, to the detriment of consumers
- Increasing DUoS tariffs, when already expecting to over recover allowed revenue, would constitute a breach of the Distribution Licence
- 40 days' notice will not allow the additional costs to be included in the Price Cap

Changing 'Final' tariffs reduces market certainty, to the detriment of consumers

As you are aware, Schedule 19 of DCUSA requires DNOs to ordinarily provide 15 months' notice of tariff changes. Market participants rely on these tariffs remaining 'final' in their retail tariff offerings to end consumers.

We acknowledge that Schedule 19 also provides for the Authority to direct a 40 day notice period – however we consider that this should only be exercised in exceptional circumstances, for example to correct a manifest error. Whilst COVID-19 itself is an exceptional issue, we do not consider the amount of NCD bad debt likely to be carried by DNOs will be exceptional.

Therefore, we do not agree with the proposal to allow DNOs to change published 2021/22 DUoS tariffs. We consider this will undo some of the benefits identified by Ofgem when it approved DCP178¹ and will add risk to future 'final' DUoS tariffs, the cost of which will ultimately be passed through to consumers. This can be avoided by allowing DNOs to recover estimated NCD bad debt in 2022/23 tariffs (subject to true-up), since these are yet to be published.

Increasing DUoS tariffs, when already expecting to over recover allowed revenue, would constitute a breach of the Distribution Licence

Under Charge Restriction Condition 2A of the Distribution Licence (Restriction of Allowed Distribution Network Revenue), DNOs are obliged to set tariffs to ensure that recovered revenue does not exceed allowed revenue:

- *2A.2 The licensee, in setting Use of System Charges, must use its reasonable endeavours to ensure that, in Regulatory Year t, Regulated Distribution Network Revenue does not exceed its Allowed Distribution Network Revenue.*

Schedule 15 of DUCSA requires DNOs to provide quarterly forecasts of their allowed and collected revenue. The most recent set of forecasts were published in August and show that, based on current tariffs, DNOs are expecting to over recover allowed revenue in 11 of the 14 licence areas in 2021/22, by an aggregate amount of £85m².

Forecast Recovery Position 2021/22 - based on current published tariffs													
ENWL	NPgN	NPgY	WMID	EMID	SWALES	SWEST	LPN	SPN	EPN	SPD	SPMW	SSEH	SSES
£8.2	-£5.3	£1.0	£10.5	£4.4	£5.4	£2.9	£16.7	£10.1	-£1.8	£7.0	£13.6	£5.4	-£0.5

Given the need for DNOs to forecast revenues and volumes 15 months in advance on a reasonable endeavours basis, over recoveries of allowed revenue are not unusual, or necessarily a breach of Charge Restriction Condition 2A.2. However, given what DNOs now know and expect for 2021/22, we consider it would be a clear breach of Charge Restriction Condition 2A.2 if a DNO increased DUoS tariffs when it already expected to over recover allowed revenue under current tariffs.

Therefore, if Ofgem is minded to consider requests by DNOs to change 2021/22 tariffs, we believe consent must be limited to those DNOs who provide assurance to Ofgem that such revised tariffs are compliant with Charge Restriction Condition 2A.2 and will not result in an over recovery of 2021/22 allowed revenue.

40 days' notice will not allow the additional costs to be included in the Price Cap

The proposed 40 days' notice for DUoS Tariff Changes will also be too late to incorporate into the Summer 2021 Price Cap. Efficient suppliers must be able to recover their costs and therefore we seek assurance from Ofgem that any additional amounts to be recovered in 2021/22 DUoS tariffs will be fully recoverable through the Default Tariff Cap.

¹ DCP178 (Notification period for a change to use of system charges) introduced the 15 month notice requirement.

² See DNO Cost Information Publications: <https://www.dcosa.co.uk/publications/>

For the avoidance of doubt, we are comfortable with the proposal to allow Transmission Networks and Gas Distribution Networks the ability to recover COVID-19 related bad debt in 2021/22 since the concerns above do not apply to these sectors.

I hope you find these comments helpful. Please contact me if you would like to discuss any aspect of our submission.

Yours sincerely,

Andy Manning
Head of Industry Transformation, Governance and Forecasting
Centrica Regulatory Affairs, UK & Ireland