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**04 February 2019**

## **Citizens Advice response to Ofgem consultation: Targeted charging review: minded to decision and draft impact assessment**

Dear Andrew,

We are pleased to be able to respond to this consultation. Citizens Advice has statutory responsibilities to represent the interests of energy consumers in Great Britain. This document is entirely non-confidential and may be published on your website. If you would like to discuss any matter raised in more detail please do not hesitate to get in contact.

In summary:

- **It's the right thing to do:** Ofgem is right to address the issues with the residual network charge. Distortions are likely to worsen as more users are able to avoid network charges through installing on-site generation. This puts an increasing burden of costs on users who are unable to take actions to reduce their network usage. Residual charges should not send signals to users to change behaviours.
- **We don't have the whole picture:** the full impact on consumers and micro-businesses is unclear with ongoing RIIO2 negotiations and the Access and Forward-Looking Charges SCR. In Ofgem's proposals for the TCR some consumers will be better off and some will lose out. We have particular concerns on the impact of non-domestic micro-businesses consumers who might see residual charges increase by 800%.
- **Dual-rate meter consumers** (Economy 7) should not face a different residual charge to single rate meter consumers. Residual charges should reflect the assets which the network user needs reflecting maximum capacity and not the volume of energy used.
- **Our preferred option** is the Agreed/Deemed Capacity Charge model which, on balance, seems preferable to the Fixed Charge model.
- **We support the reform of Embedded Benefits** which provide perverse investment signals to embedded generators.
- **Ofgem need to make decisions at the right time:** The Access and Forward-Looking Charge SCR needs to develop further before decisions are made on the TCR. An aim of this work should be to achieve an enduring solution to paying for network costs which is fit for the future. Work underway in other workstreams might have consequential impacts to the TCR proposals.

We have outlined answers to the questions in your consultation below.

**Question 1. Do you agree that residual charges should be levied on final demand only?**

Levying residual charges on final demand seems like the right thing to do if consumers end up paying for residual charges in the long run. We have not disagreed with this intent previously. However, we would like to see Ofgem demonstrate in further detail the link between residual charges to generators end up being paid by consumers.

**Question 2. Do you agree with how we have assessed the impacts of the changes we have considered against the principles? If you disagree with our assessment, please provide evidence for your reasoning.**

The approach to assessment seems to be logical.

One aspect of the Fixed Charges model which seems to have been missed is that users may choose to change LLFC to avoid a higher residual charge. This might result in higher costs for network companies in managing these requests. This is a negative consequence and does not provide a signal to users to change behaviour, which is not what residual charges should do. Similarly, larger users with Agreed Capacity (through a connection agreement with the Distribution Network Operator or Electricity System Operator) may be encouraged to alter this capacity to reduce their residual charges. This might place an adverse administrative burden on these companies, and therefore introduce costs into the process which are ultimately paid for by consumers.

**Question 3. For each user, residual charges are currently based on the costs of the voltage level of the network to which a user is connected and the higher voltage levels of the network, but not from lower voltage levels below the user's connection. At this stage, we are not proposing changes to this aspect of the current arrangements. Are there other approaches that would better meet our TCR principles reducing harmful distortions, fairness and proportionality and practical considerations?**

At a domestic and micro-business level, this approach seems reasonable. However, where larger embedded users of the network impact the transmission network there's a question as to whether these users should be subject to a proportion of the transmission residual charge. The complexity of this approach might negate the benefits, but we would encourage Ofgem to explore the fairness of continuing the current approach between transmission and large distribution users.

**Question 4. As explained in paragraphs 4.41, 4.43, 4.46, 4.49, 4.80, we think we should prioritise equality within charging segments and equity across all segments. Do you agree that it is fair for all users in the same segment to pay the same charge, and the manner in which we have set the segments? If not, do you know of**

**another approach with available data which would address this issue? Please provide evidence to support your answer.**

We agree that it is reasonable for all users to pay the same charge if the charging segments represent similar user types.

**Question 5. Do you agree that similar customers with and without on-site generation should pay the same residual charges? Should both types of users face the same residual charge for their Line Loss Factor Class (LLFC)?**

We agree that similar customers with and without on-site generator should pay the same residual charge. We do not think that residual charges should incentivise behaviours of users of the networks.

**Question 6. Do you know of any reasons why the expected consumer benefits from our leading options might not materialise?**

The analysis assumes a range of Deemed Capacity values which we believe require further explanation. Similarly, it is assumed that dual-rate meter consumers (Economy 7 and similar non-smart TOU meters) will be subject to higher charges for similar infrastructure to single-rate meter consumers which, as explained in our answer to question 8, is not fair for an essential service.

We also believe that the assumptions made for non-domestic micro-businesses, which might see rises of 800% increase in residual charges, are wrong.

All of the above will affect expected consumer benefit.

**Question 7. Do you agree that our leading options will be more practical to implement than other options?**

We agree that the leading options will be more practical to implement however, other more complex models shouldn't be completely ruled out if they deliver consumer benefit.

**Question 8. Do you agree with the approaches set out for banding (either LLFC or demanding for agreed capacity)? If not please provide evidence as why different approaches to banding would better facilitate the TCR principles.**

LLFC bands appear to be a simple and logical way to segment users, but we believe there are some challenges. Dual-rate meter consumers (Economy 7 and similar non-smart TOU meters) will see higher residual charges for similar network infrastructure is not fair for delivery of an essential service. Residual charges should take in to account the maximum capacity of the connection, and therefore the size and cost of the network assets required, and not the volume of energy used.

As noted in our answer to question 6, we would like more information on the assumptions for Deemed capacity values. Using Deemed Capacity might directly overlap with the Access and Forward-Looking Charge SCR work for 'Core Capacity'. If the Deemed Capacity option is taken forward it make sense to ensure that the capacity based charges for residual and access are aligned to reduce complexity.

**Question 9. Do you agree that LLFCs are a sensible way to segment residual charges? If not, are there other existing classifications that should be considered in more detail?**

Using LLFCs to segment residual seems logical and simple to implement, although we question the need to segment Economy 7 (and similar non-smart TOU meters) consumers differently from single-rate users. The network infrastructure costs will not be significantly different between single-rate and dual-rate users. Therefore, we believe that Economy 7 users will be penalised for having a dual-rate meter which might then send a signal to those users to move to a single-rate meter.

**Question 10. Do you agree with the conclusions we have drawn from our assessment of the following? a) distributional modelling b) the distributional impacts of the options c) our wider system modelling d) how we have interpreted the wider system modelling? Please be specific which assessment you agree/disagree with.**

We think that there is a need for further analysis here. We agree with the views put forward in the Grid Edge Policy report<sup>1</sup>, "Ofgem have not properly considered the impacts of its proposals on low incomes and whether any alternatives could have addressed its primary concern in a way which would have less damaging effects." Grid Edge Policy also suggested that a hybrid measure with a fixed charge and a supplementary charge above a certain level potentially using different approaches could be used for domestic consumers and non-domestic. We think this approach should be considered.

**Question 11. Do you agree with our proposed approach to the reform of the remaining non-locational Embedded Benefits?**

Yes. We support the reform of the remaining non-locational Embedded Benefits which provide perverse investment signals to embedded generators resulting negative impacts to consumers. The energy system should be non distortive. We have previously supported Ofgem's policy to remove embedded benefits.

Whilst we did not respond to the Small Generator Discount consultation we agree with Ofgem's decision to extend this benefit to 31 March 2021.

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<sup>1</sup> Understanding the Impacts of Ofgem's Targeted Charging Review, January 2019  
[https://docs.wixstatic.com/ugd/140d4b\\_d97aba68981041978c5367c405c1eca1.pdf](https://docs.wixstatic.com/ugd/140d4b_d97aba68981041978c5367c405c1eca1.pdf)

**Question 12. Do you agree with our proposal not to address any other remaining Embedded Benefits at this stage? Which of the embedded benefits do you think should be removed as outlined in 6.6? Please state your reasoning and provide evidence to support your answer.**

We think Ofgem should work to remove any distortions in the energy system which could provide perverse investment signals to new generation. The remaining Embedded Benefits are low in materiality but the aim should be to remove these distortions completely over time.

**Question 13. Are there any reasons we have not included that mean that the remaining Embedded Benefits should be maintained?**

No.

**Question 14. Do you agree with our proposed approach to transitional arrangements for reforms to: a) transmission and distribution residual charges b) non-locational Embedded Benefits? Please provide evidence to indicate why different arrangements would be more appropriate.**

We agree with the proposed approach to transitional arrangements for reforms to transmission and distribution residual charges. However, as we have outlined above, we believe that final decisions on the TCR should be made once the Access and Forward-Looking Charges SCR has moved on further.

We believe that reforms to Non-locational Embedded Benefits should be implemented as soon as possible. Again, there might be merit in allowing the Access and Forward-Looking SCR to move along further as some generators may be disadvantaged if Embedded Benefits are removed before new access arrangements have been agreed and implemented.

**Question 15. Do you agree with our minded to decision set out? If not please state your reasoning and provide evidence to support your answer.**

We support the overall intent of the minded to decision, but we have some concerns over the detail as set out in our answers above. We would like to see further analysis and justification and would like assurances about the impact on consumers - particularly dual-rate meter consumers and non-domestic micro-businesses. Ofgem and industry need to be able to consider proposals based on wider changes to network charging and the final RII02 deals, i.e. the whole picture, and not just the impact of an element of the network charges on consumer bills.

**Question 16. For our preferred option do you think there are practical consideration or difficulties that we have not taken account of? Please provide evidence to support your answer.**

As we have outlined above, the Fixed Charges option unfairly discriminates against dual-rate meter users and therefore it may not be practical to implement the preferred option if the LLFC groups need to be altered.

I trust that this response is clear, but would be happy to discuss any matter raised within it in more depth if that would be helpful.

Yours sincerely

**Stew Horne**

Principal Policy Manager, Energy Networks and Systems