

## Notice under section 11 of the Electricity Act 1989

### Proposal to modify the licences granted or treated as granted to SP Manweb plc and to SP Distribution Limited under section 6(1)(c) of the Electricity Act 1989

The Gas and Electricity Markets Authority (the "Authority") hereby gives notice pursuant to section 11 of the Electricity Act 1989 (the "Act") as follows:

1. The Authority proposes to modify the licences (the "SP Licences") granted or treated as granted by the Authority under section 6(1)(c) to SP Manweb plc and SP Distribution Limited to distribute electricity for the purpose of giving a supply to premises or enabling a supply to be so given.
2. The proposals are to:
  - a) amend the meaning of the ALP (the allowed loss percentage) term in paragraph 2 of Special Condition C1 (Calculation of charge restriction adjustments arising from the distribution losses incentive scheme) of each of the SP Licences, by including "to the relevant year t"; and
  - b) amend Annex A to Special Condition C1 in each of the SP Licences to introduce new ALP values for SP Manweb plc and for SP Distribution Limited, which will result in two ALP values; one for the relevant year t commencing 1 April 2005 and the other for each successive relevant year t, commencing from 1 April 2006 onwards,as set out in bold text in Annex 1 to this notice.
3. The reasons why the Authority proposes to make these licence modifications, following an investigation into compliance by SP Manweb plc with its obligations in Special Condition C1 relating to the calculating and reporting of units distributed and losses, are fully set out in:
  - a) Annex 2 (Reasons for the modification proposals) to this notice; and
  - b) *Statement by the Gas and Electricity Markets Authority, following an investigation into compliance by SP Manweb with obligations in its distribution licence relating to the calculating and reporting of units distributed and losses, January 2006, 07/06,*

copies of which are available (free of charge) from the Ofgem Library, 9 Millbank, London, SW1P 3GE (020 7901 7003) or the Ofgem website ([www.ofgem.gov.uk](http://www.ofgem.gov.uk)).

5. The effect of the proposed modifications to Special Condition C1 is to change the ALP for SP Manweb plc and for SP Distribution Limited, as follows:

	SP Manweb	SP Distribution
ALP prior to modification	7.52%	6.45%
Revised ALP for 2005/06	5.85%	5.41%
Revised ALP for 2006/07 to 2009/10	5.32%	5.13%

6. Any representations or objections to the proposed licence modifications must be made in writing on or before 7 February 2006, and should be addressed to Colette Schrier, Office of Gas and Electricity Markets, 9 Millbank, London, SW1P 3GE (0207 901 7239) or [colette.schrier@ofgem.gov.uk](mailto:colette.schrier@ofgem.gov.uk).



Martin Crouch  
 Director – Distribution, Networks  
 Authorised on behalf of the Authority

10 January 2006

***SPECIAL CONDITION C1 – Calculation of charge  
restriction adjustments arising from the distribution  
losses incentive scheme***

1. The purpose of this condition is to establish the amount of incentive that adjusts allowed demand revenue so as to reflect the performance of the licensee under the scheme set out below in respect of distribution losses.

Formula for the losses incentive adjustment (IL<sub>t</sub>)

2. For the purposes of paragraph 2 of special condition B3 (Restriction of distribution charges: total incentive revenue adjustment), IL<sub>t</sub> is calculated in accordance with the following formula:

$$IL_t = [LR \times PIAL_t \times (AL_t - L_t)] + \left[ PLR \times PIAL_t \times \left( 1 + \frac{ALP}{100} \right) \times PVL_t \right]$$

where:

LR is the distribution losses incentive rate and takes the value of £48/MWh for units physically distributed on or after 1 April 2005.

PLR is the previous distribution losses incentive rate and takes the value of £32.24/MWh for units physically distributed before 1 April 2005.

PIAL<sub>t</sub> is the price index adjustment, which in the relevant year commencing 1 April 2004 takes the value of 1, and in each subsequent relevant year is derived from the following formula:

$$PIAL_t = \left[ 1 + \frac{RPI_t}{100} \right] \times PIAL_{t-1}$$

L<sub>t</sub> means, in respect of the relevant year t, the adjusted distribution losses calculated in accordance with the methodological basis set out in paragraphs 3 to 5 and 9.

AL<sub>t</sub> means an amount representing the benchmark level of distribution losses in the relevant year t calculated, subject to paragraphs 6 to 8 below, in accordance with the following formula:

$$AL_t = \frac{ALP}{100} \times AUD_t$$

where:

ALP is the allowed loss percentage and shall, unless the Authority has directed otherwise in accordance with paragraph 7, take the value set against the licensee's name **for the relevant year t** in Annex A.

AUD<sub>t</sub> means, in respect of the relevant year t, the adjusted units distributed as defined in paragraph 5.

PVL<sub>t</sub> means the number of units distributed recorded by the licensee, in respect of the relevant year t, that were physically delivered before 1 April 2005, and where the adjustment may be positive or negative.

RPl<sub>t</sub> is determined in accordance with paragraph 4 of special condition B1 (Restriction of distribution charges: demand use of system charges).

### **Basis of calculation of adjusted distribution losses (L<sub>i</sub>)**

3. Adjusted distribution losses shall be deemed to be the difference between adjusted system entry volumes and adjusted units distributed.
4. Adjusted system entry volumes shall be equal to the sum of:
  - (a) all units metered on entering the licensee's distribution system;
  - (b) all units deemed to be entering the licensee's distribution system by entry points that are unmetered; and
  - (c) an amount (in units) representing the excess adverse effect on losses (DGA<sub>i</sub>) of units entering the system at entry points (other than entry points which are connected to an onshore transmission network) where the loss adjustment factor applied for settlement purposes is less than 0.997, as calculated by the following formula:

$$DGA_t = \sum (LAF_{it} - 0.997) \times DGV_{it}$$

where:

$$LAF_{it} = \min(LAG_{it}, 0.997)$$

DGV<sub>it</sub> is the total number of units, in respect of the relevant year t, entering the distribution system at entry point *i*; and

LAG<sub>it</sub> is the value, in the relevant year t, of the loss adjustment factor applicable to entry point *i*.

5. Adjusted units distributed shall be equal to:
  - (a) the sum of:

- (i) all units distributed by the licensee metered at exit points on leaving the licensee's distribution system, and
  - (ii) all units deemed to be leaving the licensee's distribution system at exit points that are unmetered;
- (b) but excluding:
  - (i) the units, whether metered or unmetered, recorded as distributed by the licensee and that were physically delivered before 1 April 2005, and
  - (ii) in respect of Scottish Hydro-Electric Power Distribution Limited, also those units deemed to be leaving the licensee's distribution system at shared unmetered exit points.
- 6. Subject to paragraph 7, the value of ALP set against the licensee's name in Annex A shall apply so long as this condition continues in force.
- 7. The Authority, having due regard to the purpose of this condition, and being satisfied, following consultation with the licensee, that there has been a material change (whether an improvement or a deterioration) in the quality of the information used to derive the adjusted system entry volumes or adjusted units distributed, may, with the licensee's consent (which shall not be unreasonably withheld), direct the licensee to change the value of ALP, to which paragraph 6 refers, to a different value specified by the Authority.
- 8. A change to the value of ALP in accordance with paragraph 7 may be directed by the Authority at any time during the year but shall not take effect before the beginning of the relevant year commencing immediately after the date of the direction.
- 9. The licensee shall, unless otherwise agreed by the Authority, calculate each component of adjusted distribution losses for the relevant year t on the same basis as that used within the calculation of adjusted distribution losses in respect of the relevant year commencing 1 April 2002, pursuant to paragraph 7 of special condition D (Information to be provided to the Authority in connection with the charge restriction conditions), or in Scotland special condition E, of this licence in the form in which it was in force on 31 March 2005.

### Annex A: Value for ALP by licensee

<b>Licensee</b>	<b>ALP</b>
Central Networks West plc	4.96
Central Networks East plc	5.69
United Utilities Electricity plc	5.68
Northern Electric Distribution Limited	5.20
Yorkshire Electricity Distribution plc	5.90
Western Power Distribution (South West) plc	6.96
Western Power Distribution (South Wales) plc	4.94
EDF Energy Networks (LPN) plc	6.54
EDF Energy Networks (SPN) plc	6.54
EDF Energy Networks (EPN) plc	6.32
<b>SP Distribution Limited</b>	<b>6.45</b>
<b>SP Manweb plc</b>	<b>7.52</b>
Scottish Hydro-Electric Power Distribution Limited	8.73
Southern Electric Power Distribution plc	6.74

**For SP Distribution Limited, ALP shall take the value:**

- **5.41 for the relevant year t commencing 1 April 2005**
- **5.13 for the relevant year t commencing 1 April 2006 and every subsequent relevant year t.**

**For SP Manweb plc, ALP shall take the value**

- **5.85 for the relevant year t commencing 1 April 2005**
- **5.32 for the relevant year t commencing 1 April 2006 and every subsequent relevant year t.**

## **Annex 2 (Reasons for the modification proposals) to Notice under section 11 of the Electricity Act 1989**

- a) In the period 2001/2 to 2003/4, the SP licensees each reported values for units distributed based on assessments of losses derived independently of settlement data. Subsequent settlement data has demonstrated that actual units distributed were substantially higher than these reported values, and hence losses were substantially lower than the reported values. The difference between reported and actual units (based on settlement data) and corresponding differences in use of system charges were held by the SP licensees on their balance sheets until the end of the settlement process.
- b) The difference between reported losses and losses implied by settlement data on average over the three-year period 2001/02 to 2003/04 has been calculated and is as set out in Table 1 below.

Table 1: difference between reported and actual losses (using settlement data) for the 3 year period April 2001 to March 2004 (in percentage points)

Based on settlement data as at:	SP Manweb	SP Distribution
July 2004	1.67%	1.04%
March 2005	2.20%	1.32%

- c) Ofgem<sup>1</sup> considers that it would have taken into account the actual losses performance from 2001/02 in the setting of the SP licensees' ALP for 2005-10 had it been aware of the size of settlement provisions at the time of the setting of the price control. The Authority therefore proposes to reduce the values of ALP pertaining to the SP licensees by the amounts set out in Table 1. The Authority considers that settlement data from 31 July 2004 should be used to adjust the value of ALP for 2005/06 and data from 31 March 2005 for subsequent years.
- d) Ofgem does not propose to make any modifications to Special Condition C1 relating to the treatment of units distributed prior to 1 April 2005 because the SP Licensees have each agreed to restate such units, based on settlement data to a date to be agreed with the Authority, to the year in which they relate.

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<sup>1</sup> Ofgem is the office of the Authority.