



Commission for Energy Regulation

An Coimisiún um Rialáil Fuinnimh

**Determination of Distribution Allowed
Revenues and Distribution Use of System
Tariffs for 2005**

Draft Decision

**CER 04/294
10th September 2004**

DISTRIBUTION USE OF SYSTEM CHARGES 2005

Introduction

Section 36 of the Electricity Regulation Act, 1999 requires the Commission to approve the statement of charges for the use of the distribution system. These charges are required to defray the costs incurred by ESB Networks in its capacity as licensed Distribution System Operator. These costs include the day-to-day operation of the system and remuneration of the major capital investment programme which is currently under way. The formula to calculate the revenue to recover such costs is set out in the Commission's determination of Distribution Allowed Revenues.¹

The Commission proposes to approve revenues of €592.29 million to be earned by the Distribution System Operator in 2005. This results in an increase in Distribution Use of System (DUoS) charges of 2.1% in 2005 from 2004.

The approved revenue takes into consideration various adjustments required in the revenue formula such as: inflation, pass-through costs and incentives/penalties for meeting targets set in the revenue formula for improvements in customer minutes lost and reductions in electrical losses on the distribution system. The revenue is also adjusted to account for growth in customer numbers and throughput; in 2005 customer numbers and throughput are forecast to rise by 3.4% and 3.8% respectively on 2004 figures. In addition, since the initial revenue determination, the Commission has approved expenditures on a number of items, including market opening, business separation and acceleration of refurbishment of the distribution networks and installation of bulk supply point metering. The various components making up the overall revenue are described in more detail in the sections below.

Distribution Revenue Determination 2001-2005 €557.6 million:

In 2001 the Commission determined the level of allowed revenues for the Distribution System Operator for the period January 2001 to December 2005. This determination specifically set out the allowed revenues for each of the five years, including 2005. The allowed revenue for the DSO is €557.6 million in 2005 prices.

Network Acceleration €20.4million:

In May 2003 the Commission approved additional expenditure to accelerate investment in the Distribution Network. The impact of this expenditure on the 2005 revenue requirement is the addition of €20.4million to the revenue requirement for 2005.

¹ "Determination of Distribution Allowed Revenues" published in September 2001 which covered the 2001-2005 major capital investment programme which is currently underway.

The benefits that will be delivered by the approved renewal programme include the renewal of the entire medium voltage network by the end of 2005, the refurbishment of the 38kV network and the replacement of 38kV substations. The Commission expects that the approved expenditures will deliver a distribution network in line with European standards through improved quality of supply, public safety and increased network capacity.

Business Separation €3.65 million:

In July 2003, the Commission approved a comprehensive Business Separation Implementation Plan covering the necessary short and long-term solutions for business separation. The allowed revenue for operational and capital expenditure for business separation in 2005 is €3.65 million

Bulk Supply Point Metering €0.47 million:

Allowed operational and capital costs for 2005 are €0.47 million. This metering will facilitate the future calculation of Distribution system losses which can be applied to the loss reduction incentive.

Load Profile Project €1.12million:

In 2002 the Commission approved a project comprising the installation of 1800 profile meters in order to facilitate the development of profiles of customer consumption for the Irish electricity market at a total cost of €5.48million. The impact of this project on the 2005 revenue requirement is an additional €1.12million.

Market Opening IT €6.9 million:

Expenditure on this item was approved to facilitate the replacement of the interim DUoS billing system, the updating and replacing of the meter and data collections systems, and to facilitate the change of supplier process for full market opening. Additional approved expenditure was offset by deferred expenditure on other previously approved IT projects. The net impact of this expenditure is an additional €6.9 million on the revenue requirement for 2005.

Penalties -€12.08 million:

In accordance with the allowed revenue formula, the Commission has imposed a penalty of €12.08 million for the failure of meeting the targets set by the Commission for reductions in electrical losses on the distribution system. No penalty or reward was imposed with regard to customer minutes lost as the benchmark target is expected to be met in 2005. The level of the penalty was at the maximum of 2% of allowed revenues in the year.

Deferral -€11.41 million:

In the 2005 Determination of ESB Power Generation's (ESBPG's) Allowed Revenues the Commission minimised the substantial under-recoveries of 2003/2004 to be carried over beyond 2005. In its submission for 2005 ESB provided the Commission with details of a €196m under-recovery comprising mainly of differences between actual and forecast fuel costs. Minimising

under-recoveries is considered to be in the final customers' long-term interest as it avoids expensive interest payments accruing on the under-recovered amount. It is also of considerable importance that the contestable generation sector can operate in a cost reflective manner. This helps ensure a level playing field.

The Commission must, on the other hand, take a balanced view when considering the resulting impact in the end-user tariff. For this reason the Commission's decision to substantially reduce ESBPG's under-recoveries still leaves a need for a smaller deferral of €29.91m (2005 prices) of revenue accruing to the non-contestable networks' component of ESB's business, ESB Networks. The Commission apportions this deferral by way of €11.41m of the distribution allowed revenue and €18.50m of the transmission allowed revenue. The Commission considers that this is an appropriate and important means of ensuring more cost-reflective prices from the contestable generation sector.

On this basis the Commission defers €11.41m (2005 prices) of the DSO's revenue for 2005. This deferral will be taken into account in the next multi-annual Distribution Price Control which will take effect from 2006.

Balance:

The balance of the revenue requirement was made up of underrecoveries from previous years and adjustments to the allowed revenue allowed based on projected customer numbers, in line with the formula contained in the Determination of Distribution Allowed Revenues.

Under recoveries in 2003 and 2004 came to €13.5 million and €8.3 million respectively. The 2003 under recovery was mainly due to actual 2003 turnout for dismantling costs and non-repayable diversions being higher than originally estimated in the Distribution Allowed Revenues. Dismantling costs refer to the retiring of existing network due to upgrading work on the network or new connections. Non-repayable line diversions arise whereby overhead lines or cables are diverted in order to allow developments or building on private property. Regarding the 2004 under recovery, revised forecasts for 2004 customer numbers were higher than the forecast made last year for 2004; the revenue requirement was revised upwards by €3.4 million to take account of this. Additionally, customer minutes lost are expected to be lower than the figure forecast in the 2004 revenue formula, resulting in an upward adjustment of revenue of €6.7 million.

Customer numbers for 2005 are also expected to be 34,000 higher than originally envisaged in the Distribution Revenue Formula, with a resultant addition of €2.7 million to required revenue for 2005.

Tariff Impact:

The revenue requirement of €592.29 million has resulted in an increase in the average unit price of 2.1%, which is below forecast inflation, in the Distribution Use of System Tariff. While the allowed revenue has increased by 7.7%, the energy throughput in 2005 is expected to increase by 5.4%.

These figures are based on the forecast throughput for 2004 made in the 2004 allowed revenue formula, on which 2004 tariffs were set, and the forecast throughput for 2005 on which 2005 tariffs are set.

Please click here (<http://www.cer.ie/CERdocs/cer04301.pdf>) to view: The proposed Schedule of Distribution Use of System Charges 2005.

DUoS Rules:

Also published today is the ESB Networks paper entitled “Rules for Application of DUoS Tariff Group”. In the context of full market opening, there was a need to clearly set out the basis for the application of the Distribution Use of System Tariffs and Public Service Obligations. This document, approved by the Commission, addresses this need and outlines the rules for applying the correct Distribution Use of System (DUoS) tariff (DUoS Group) to a customer premises or connection point.

It also outlines the requirements for new connections or a new customer at an existing connection point (Change of Legal Entity) in addition to addressing specific issues concerning existing connections.

Please click here (<http://www.cer.ie/CERdocs/cer04300.pdf>) to view: “Rules for Application of DUoS Tariff Group”.

For further information contact Aidan Kearney at the Commission, e-mail akearney@cer.ie