

Electricity network charges in Great Britain – submission from Ofgem to Convention of the Highlands and Islands. 17 October 2016

Ofgem's role

Ofgem is the Office of Gas and Electricity Markets. We are the independent regulator of the electricity and gas system in Great Britain and our principal objective is to protect the interests of existing and future energy customers. This note provides a brief overview of the current network charging regime, the implications of a move to national network charges and some other considerations regarding regional differences in network charges and electricity bills.

Current distribution network charging regime

Network charges recover the costs of operating and investing in the transmission and distribution networks. The network owners recover these costs from generators and also from suppliers who in turn include the charges as part of the overall bill they issue to their customers. The costs of running these networks vary due to a range of factors including the geography of a region, the number of customers, and the level of new investment required.

These charges and the range of regional differences vary year on year. For example, distribution charges for consumers on single rate meters with typical consumption of 3,100 kWh per year¹, ranged from £66 to £122 in 2015/16 whereas for 2016/17 the range is £67 to £137 per year. The range for electricity transmission charges for similar consumers was £21 to £37 in 2015/16 and £35 to £41 in 2016/17. Gas network charges also vary year on year.

Implications of a national approach to network charging

In 2015, we reviewed regional differences in network charges based on a snapshot for the charging year 2015/16.² As part of our analysis we illustrated the potential impact of moving to Great Britain wide network charges for both electricity and gas. For that charging year, it would have meant approximately 16m households would have faced higher network charges, while around 11m would have seen reduced charges across GB. In Scotland, 1.8m customers in the South of Scotland would have faced higher network charges, while 0.7m customers in the North of Scotland would have faced reduced charges. In most cases, including within Scotland, the increase or decrease would have been small, less than £20, for a typical customer. As network charges vary from year to year for each charging zone, this can change the degree of potential gain or

¹ A single rate consumer is one who is charged on the basis of p/kWh regardless of time of day. The median consumption level for such consumers in Great Britain is about 3,100 kWh per year.

² Regional differences in network charges:
https://www.ofgem.gov.uk/sites/default/files/docs/2015/10/reg_charges_final_master_version_23_october_2015.pdf

loss that would result from national network charges for individual consumers across Great Britain.

We also considered the distribution of customers in vulnerable situations across the different distribution regions, finding no clear justification for national network charges in terms of regional concentration of vulnerability. We also explained that there are regulatory advantages in charges that broadly reflect the costs that different users place on the system. However, a decision to move to a socialised approach is a matter for Government to decide.

Hydro Benefit Replacement Scheme and Common Tariff Obligation:

There are two mechanisms in place to protect consumers from the relatively higher costs of running the electricity distribution network in the North of Scotland region. One is the Hydro Benefit Replacement Scheme (HBRS) which provides an average annual subsidy of about £30 for a typical domestic customer in the North of Scotland.

Secondly, there is the Common Tariff Obligation (CTO) scheme, which protects consumers from the higher costs of supplying electricity to remote areas and islands. The CTO means that suppliers are not able to charge comparable domestic consumers different prices on the basis of their location within a particular electricity distribution area. For example, suppliers must offer the same tariffs to customers in Aberdeen and in Assynt.

Supplier pricing

Pricing strategies are a strategic decision for suppliers, and regional differences in network charges are only one of the factors that determine the differences in tariffs offered by electricity suppliers. Ofgem's analysis and the conclusions of the recent investigation by the Competition and Markets Authority have found that customers who remain on standard variable tariffs are paying substantially more - currently around £300 for a typical customer - for the energy that they use compared to those who switch to the cheapest deals.³

³CMA Energy Market Investigation. The Pricing Strategy of the Six Large Energy Firms https://assets.publishing.service.gov.uk/media/54f48e7840f0b61427000009/Retail_-_pricing_strategies.pdf