

<b>Title: Widening the scope and application of the Second Comer Regime</b>  <b>IA No: DECC0200</b>  <b>Lead department or agency:</b> Department of Energy and Climate Change (DECC) <b>Other departments or agencies:</b>	<b>Impact Assessment (IA)</b>			
	<b>Date: 03/12/2015</b>			
	<b>Stage: Final</b>			
	<b>Source of intervention: Domestic</b>			
	<b>Type of measure: Secondary legislation</b>			
<b>Contact for enquiries:</b> Birgit.Wosnitza@decc.gsi.gov.uk				
<b>Summary: Intervention and Options</b>				<b>RPC: Green</b>

Cost of Preferred (or more likely) Option				
Total Net Present Value:	Business Net Present Value:	Net cost to business per year	In scope of One-In, Two-Out?	Measure qualifies as
-£0.48m	-£0.48m	£0.06m	Yes	IN

**What is the problem under consideration? Why is government intervention necessary?**

The Electricity Connection Charges Regulations 2002 (ECCR) (also known as the 'Second Comer Regime') are designed to ensure the cost of connecting to the electricity distribution network is shared fairly between different parties. Specifically, the regime provides that where a party (the 'second comer') connects to and benefits from infrastructure that was paid for by an earlier party, the second comer must reimburse the earlier party (initial connectee and/or the distribution network operator (DNO)) for a proportionate share of the costs. However, the earlier party is only entitled to a reimbursement if the initial connection has been provided by the local monopoly provider, the DNO or independent distribution network operator (IDNO). In addition, the right of reimbursement to where a second comer connects within five years of the initial connection being made. This is likely to cause *economic inefficiencies* due to creating barriers to entry and expansion for independent connection providers (ICPs). This might obstruct competition and economic growth. There is also a perceived *equity concern* as costs are currently not shared fairly between some parties. This barrier to entry and expansion might obstruct competition and economic growth. In order to amend the scope of the Second Comer Regime, secondary legislation is needed.

**What are the policy objectives and the intended effects?**

The two key policy objectives of widening the scope and application of the Second Comer Regime are:

To **support competition in the connections market**, by ensuring greater parity between different connection providers. Government believes competition in connections can play a valuable role in giving customers greater choice and helping to drive up performance across the network industry (e.g. improved customer service). It also signals Government's support for small and medium sized enterprises (SMEs) as ICPs tend to be smaller companies.

To ensure **fairer sharing of costs between parties**, including those who choose not to use a DNO/ IDNO for their connection. Second comers should be required to pay a proportionate contribution to infrastructure paid for by an earlier party, regardless of who provided the initial connection or the type of connection agreement used. The regime should apply for as long a time period that is reasonably practicable to administer.

**What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)**

Two options have been considered:

- 'Do Nothing': Status Quo (i.e. continue with the existing Second Comer Regime)
- 'Policy Option': Widen the scope and application of the Second Comer Regime to include connections: by ICPs; between distribution systems; using Section 22 agreements (e.g. a consortium of connectees); and extend the time limit from five to 10 years after the initial connection was made.

The 'Policy Option' is preferred as it will help ensure fairer cost sharing regardless of who a customer uses to provide its connection, the type of connection and for a longer time period. The policy change will support competition in electricity connections and improve equity. There is no other effective means of widening the scope and scale of the Second Comer Regime, and the status-quo would perpetuate the current inequality between connection providers.

<b>Will the policy be reviewed?</b> It will be reviewed. <b>If applicable, set review date:</b> 5 years after commencement					
Does implementation go beyond minimum EU requirements?			N/A		
Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.	<b>Micro Yes</b>	<b>&lt; 20 Yes</b>	<b>Small Yes</b>	<b>Medium Yes</b>	<b>Large Yes</b>
What is the CO2 equivalent change in greenhouse gas emissions? (Million tonnes CO2 equivalent)	Traded: N/A		Non-traded: N/A		

***I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.***

Signed by the responsible Minister:---- Jesse Norman Date: 6 February 2017

# Summary: Analysis & Evidence

# Policy Option

Description: Widen the scope and application of the Second Comer Regime.

## FULL ECONOMIC ASSESSMENT

Price Base Year: 2014	PV Base Year: 2015	Time Period Years: 10	Net Benefit (Present Value (PV)) (£m)		
			Low: -0.08 (highest net benefit)	High: -1.45 (lowest net benefit)	Best Estimate: -0.48

COSTS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	n/a	0.17	1.39
High	n/a	7.12	59.25
Best Estimate	n/a	1.75	14.54

### Description and scale of key monetised costs by 'main affected groups'

The overall cost associated with the proposed policy change is estimated to be low. The text below sets out the monetised costs by main effected groups (further detail can be found in the supporting evidence):

- **Additional costs for second comers** that connect to ICP-built connections within 10 years from the initial connection being made and to DNO/ IDNO-built connections between five and 10 years of the initial connection being made. This represents an additional transfer from second comers to initial connectees and DNOs where wider network reinforcement was required. The additional average annual cost (best estimate) is estimated to be £1.69m (cost, 2014 prices). This represents a transfer from second comers to first comers.
- **Additional administrative costs for DNOs/ IDNOs.** These costs are associated with processing second comer payments and incurred on issuing quotes and completing connection invoices. The additional average annual cost (best impact) is estimated to be £0.06m (cost, 2014 prices). These costs are passed through to initial connectees.
- **Additional potential appeal costs for Ofgem.** Ofgem (the independent network regulator) acts as final arbitration point if customers are unhappy with the price charged for a connection (or reinforcement), this can include any second comer element of the connection cost. The additional average annual cost (best impact) is estimated to be £125 (cost, 2014 prices). Costs are passed through to the System Operator, DNOs and gas distribution networks.

### Other key non-monetised costs by 'main affected groups'

- Additional transfer costs for second comers that connect to connections between distribution systems or connections using a Section 22 agreement (transfers); these are likely to be small due to their rare occurrence.
- Additional administrative costs to DNOs/IDNOs of processing second comer payments in relation to connections between distribution systems or connections using a Section 22 agreement.
- A more level playing field for ICPs may increase the connections business won by ICPs and correspondingly reduce the business won by DNOs. It is not possible to quantify this cost to DNOs. Overall, it is likely to be small as there are a range of factors that determine whether a customer wishes to use non-DNO providers.

BENEFITS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	n/a	0.16	1.31
High	n/a	6.95	57.79
Best Estimate	n/a	1.69	14.06

**Description and scale of key monetised benefits by ‘main affected groups’**

The text below sets out the monetised benefit anticipated from the policy change (further detail can be found in the supporting evidence):

- **Additional reimbursements for initial connectees** within 10 years of the initial connection (if the initial connection was provided by an ICP) and between five and 10 years after the initial connection (if the initial connection was provided by the DNO/ IDNO). The additional average annual benefit (best estimate) is estimated to be £0.24m (benefit, 2014 prices). This represents a transfer from second comers to first comers.
- **Additional reimbursements for DNOs** for wider reinforcement within 10 years of the initial connection (if the initial connection was provided by an ICP) and between five and 10 years after the initial connection (if the initial connection was provided by the DNO/ IDNO). The additional average annual benefit (best estimate) is estimated to be £1.45m (benefit, 2014 prices). This represents a transfer from second comers to DNOs.

**Other key non-monetised benefits by ‘main affected groups’**

- **Widening the scope and scale of the Second Comer Regime should help support competition in the connections market.** This is beneficial for smaller players in the market and benefits customers as healthier competition in the connections market gives greater choice and drives up performance across the industry (e.g. improved customer service). It is not possible to quantify this benefit. Overall, it is likely to be small as there are a range of factors that determine whether a customer wishes to use non-DNO providers.

**Key assumptions/sensitivities/risks****Discount rate:** 3.5%

- There is no evidence on the number of second comer payments that would have happened but didn't because of the limited scope of the Second Comer Regime. Therefore, assumptions and sensitivities on the number of second comer payments has been drawn from the historical number of second comer payments on DNO/ IDNO-built connections and stakeholder feedback (Annex 1). The supporting evidence sets out all assumptions and sensitivities in detail.

**BUSINESS ASSESSMENT (Policy Option) (2014 prices, 2015 NPV base year)**

Direct impact on business (Equivalent Annual) £m:			In scope of OITO?	Measure qualifies as
<b>Costs: £1.69m</b>	<b>Benefits: £1.63m</b>	<b>Net impact: -£0.06m</b>	Yes	IN

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## Background

1. Obtaining a timely and affordable connection to the electricity distribution network is essential for the UK's growth and energy objectives. It means that customers, including private citizens, generators, house-builders, and commercial property developers, get access to the network to either supply to or take electricity from the grid when they need to.
2. When a new connection is made to the distribution network, a customer is required to pay for the infrastructure required to accommodate it. This can include the sole use connection (i.e. infrastructure used purely to connect the property or generator to the network) and a share of any wider network reinforcement work that may be required. Depending on the requirements of the connectee this can be costly. It is right therefore that where a later connectee connects to the infrastructure paid for by an earlier party, that they should be required to make a contribution to the cost.
3. The Electricity Connection Charges Regulations 2002 (ECCR), also known as the Second Comer Regime, are designed to ensure the cost of connecting to the electricity distribution network is shared fairly between different parties (i.e. the end-user, for example, a house, factory, generator). Specifically, they provide that where a party ('second comer') connects to and benefits from infrastructure that was paid for by an earlier party, the second comer must reimburse the earlier party for a proportionate share of the costs. The regime was introduced to help avoid subsequent connectees 'free-riding' on infrastructure paid for by someone else. The local monopoly provider, the distribution network operator (DNO) (or in some instances, an independent distribution network operator (IDNO)<sup>1</sup>), processes the second comer transfers between different parties.
4. Second comer transfers may be made to an individual customer or a DNO. The latter scenario will occur when the initial connectee's connection has prompted wider reinforcement of the network that can only be carried out by the DNO. Due to the standardised size of some network infrastructure, on occasions, the DNO may need to reinforce the network beyond that specifically needed for the initial connectee. In this case, the initial connectee will be charged a share of the reinforcement costs in line with the capacity needed to accommodate them. The rest will be paid for by the DNO<sup>2</sup>, which will then in turn pass the costs through to generation and demand customers, i.e. suppliers and generators, which, in turn, pass the costs through to end-consumers through network charges and electricity prices, respectively. Where a second comer payment is made to a DNO, it can then use it to offset network charges for suppliers and generators, therefore reducing costs to end-consumers. This represents a transfer from second comers to DNOs and ultimately to end-consumers.
5. Whilst DNOs/ IDNOs are responsible for administering the process, Ofgem (the independent network regulator) act as the final arbitration point if customers are unhappy with the price charged for a connection, this can include any second comer element of the connection cost. This has happened once over the last 13 years. Ofgem also captures information on the number of second comer payments made, as part of the annual DNO data reporting cycle.

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<sup>1</sup> There are two types of distribution systems; distribution network operators (DNOs) and independent distribution network operators (IDNOs). DNOs cover 14 specific geographical regions of Great Britain and own and operate the network within their territory. IDNOs own and operate smaller networks located within the areas covered by the DNOs – IDNO networks are mainly extensions to the DNO network. There are currently seven licenced IDNOs and they are regulated broadly in the same way as DNOs, but their licences don't have all of the conditions that a larger DNO does.

<sup>2</sup> To note, this scenario only applies in relation to DNO networks and not IDNO networks, which are much smaller.

## **Problem under consideration and rationale for Government intervention**

6. The current scope of the Second Comer Regime is limited. It only applies where a connection is provided by the local monopoly provider, the distribution network operator (or an independent distribution network operator), and there is a five year time limit. It doesn't apply where an initial connectee customer: opted to use an independent connection provider (ICP) (further explained below); connected through a Section 22 agreement (e.g. a consortium of connectees); or where a connection is made between distribution systems. Some DNOs have also requested greater clarity as to the application of the regime where the initial connection included wider reinforcement that was paid for by the DNO (and passed through to suppliers/generators through network charges and then further passed on to end-consumers through network charges and electricity prices, respectively, as set out in paragraph 4).

### *Independent connection providers (ICPs)*

7. In 2000, competition was introduced in electricity distribution network connections, to provide greater choice for customers and help drive up performance across the network industry. This means that customers can opt to use an ICP to provide their network connection, instead of the local monopoly network operator, the DNO, or an IDNO. Where an ICP builds a network connection, once complete, the infrastructure is subsequently adopted by the local DNO.
8. The Second Comer Regime currently only applies where a customer uses the local DNO/IDNO to provide the initial connection. It does not apply where a customer used an ICP. This was not a deliberate exclusion, but is due to the fact that ICPs did not exist in any significant numbers when the original legislation was drafted, so it therefore makes no explicit provision for them.
9. This is likely to cause *economic inefficiencies* due to creating barriers to entry and expansion for independent connection providers as customers may prefer to use a DNO/IDNO in order to have a chance of receiving a second comer payment. This might obstruct competition and economic growth. There is also a perceived *equity concern* as costs are currently not shared fairly between some parties.
10. Overall the scale of the problem is likely to be small as the size of the average second comer payments is low and there are relatively few payments made. However, Government believes the legislation should be updated. The omission of ICP connections is now an anomaly and a result of competition only becoming a significant factor in the market after the original legislation was drafted. Given that this could create barriers to entry and expansion for ICPs, customers that use an ICP should be made eligible for second comer payments and therewith be put on a more equal footing with DNOs/IDNOs in respect of the Second Comer Regime.
11. Whilst this inequity is generally unlikely to be a *determining factor* for a customer when deciding to use an ICP or DNO to provide a connection, some stakeholders have reported that they have considered it and that it has been a *contributing factor*. Therefore, in line with Government's objective to support competition in the connections market, the regime should be updated to help level the playing-field. There has been widespread support from stakeholders, including developers, ICPs and DNOs, for bringing ICPs within scope of the regime.
12. Government therefore proposes to bring connections made by ICPs within scope of the regime and enable DNOs to estimate the costs (relating to these types of connections).

### *Time limit extension*

13. Under the current regime, second comer payments only apply where a second connection is made within five years of the first connection. The original time limit was set at five years to manage the administrative burden and practicalities placed on DNOs of processing payments over a longer timeframe.
14. Any time limit is likely to cause *economic inefficiencies* and perceived *equity concerns* as it implies that costs are not shared fairly between parties beyond the time limit. A key concern is that a five year time period is too short to capture a full economic cycle with down and up-turns in commercial development, reducing the chance that a first comer would receive a fair contribution to their initial payment from future connectees that benefit from the infrastructure the initial connectee paid for.
15. With this in mind, Government sought views on the current five year time limit; whether the time limit can be reasonably extended (bearing in mind the potential trade-off against increasing administrative costs and complexity), and, if so, to what period. The (largely

qualitative) evidence was that the current regime was now to an extent more straightforward to administer than at the outset of the scheme due to improved record-keeping (e.g. computer systems) and that the cost of administering the scheme over a longer timeframe would remain flat (up to a point).

16. Whilst some stakeholders argued the time period should be unlimited, most stated that a time limit was, however, still necessary to limit the administrative burden and that over a longer period it would be unlikely that second comer payments would be made as any additional capacity on the initial connectee's connection would most likely have been fully utilised by second comers by that date. There was a broad view that the time period was unduly short, and that it could be extended to 10 years without increasing administrative costs substantially. Beyond this, stakeholders assessed that the costs of administration would increase exponentially and there would be diminishing likelihood of payments ever falling due, due to capacity being utilised already. Some stakeholders argued that the time limit should remain at five years.
17. Government supports the principle of the Second Comer Regime and believes that fairer cost sharing should apply regardless of the time elapsed. However, it also recognises that the administrative burden and practicalities of making the payments increases over time and therefore a time limit is necessary. Striking the perfect balance between maximising the opportunity for a fairer sharing of costs, with the need to contain the administrative complexity, is difficult.
18. Based on the evidence provided by stakeholders, drawing on feedback received during discussions and from responses to the informal consultation, Government has decided to extend the period to 10 years, as it is concerned that the five year time limit risks not covering a full economic cycle with down and up-turns in commercial development, but that a time limit longer than 10 years risks becoming impractical to administer and the likelihood of payments becoming increasingly unlikely due to capacity being utilised over time.

#### *Connections between distribution systems*

19. There are two types of distribution systems; distribution network operators (DNOs) and independent distribution network operators (IDNOs). DNOs cover 14 specific geographical regions of Great Britain and own and operate the network within their territory. IDNOs own and operate smaller networks located within the areas covered by the DNOs – IDNO networks are mainly extensions to the DNO network. There are currently seven licenced IDNOs and these are regulated in the same way as DNOs but their licences don't have all of the conditions of DNOs.
20. Under the existing regime, a connection that is made on a link between a DNO and IDNO network is not eligible for a second comer payment. Not including connections between distribution systems is likely to cause *economic inefficiencies* due to creating barriers for connections between distribution systems as customers may prefer other connections covered by the Second Comer regime. There is also a perceived *equity concern* as costs are not shared fairly between some parties. Government therefore proposes to bring connections between distribution systems within scope of the regime. Overall the scale of the problem is likely to be negligible; there are only a few connections between distribution systems a year, and the chance of second comer payments being due is very low.

#### *Section 22 connections*

21. Sections 16 to 17 of the Electricity Act set out the legal requirements on network companies to provide a connection to the distribution network. These provisions require a DNO/ IDNO to specify what information a customer must provide, the payment they must make, the security requirements and other relevant terms the customer will need to accept. The vast majority of connections are made through a Section 16 connection request.

22. Section 22 of the Act also includes a provision for a DNO/ IDNO to agree more flexible terms with the connection customer that are not bound by some of the regulatory requirements, which Section 16 requests are bound by. This, for example, could be used where a group of connectees looking to connect in the same part of the network come together to form a consortium, as a means of sharing connection costs. Section 22 provisions provide alternative arrangements so that a DNO/ IDNO can consider customers' collective requirements and deliver a combined scheme that reduces the cost and timeframes for all.
23. As the current ECCR are centred around Section 16 connection requests, Section 22 agreements also do not qualify for second comer payments. This is likely to cause *economic inefficiencies* due to creating barriers for connections using a Section 22 Agreement as customers may prefer other connections that are covered by the Second Comer regime. There is also a perceived *equity concern* as costs are not shared fairly between parties. Government therefore proposes to bring Section 22 connections within scope of the regime. Overall the scale of the problem is likely to be negligible: there are only a few connections using a Section 22 agreement a year.

#### *Wider reinforcement costs*

24. Some connections trigger the need for reinforcement of the wider network. The application of the 'Cost Apportionment Factor'<sup>3</sup> in relation to reinforcement means that initial connectees triggering wider reinforcement are not always required to cover the cost of *all* network reinforcement. In these scenarios, the remaining costs are paid by the DNO, who then recover the cost through networks charges passed through to electricity generation and demand customers (i.e. generators and suppliers) - Distribution Use of System (DUoS) charges – which in turn pass these through to end-consumers.
25. Currently, in the vast majority of cases, the DNOs already apply the second comer rule (for second comers up to five years after the initial connection provided by a DNO) with respect to these DNO incurred costs (for wider reinforcement). This means that where a DNO receives a second comer payment (as a reimbursement for the costs of wider reinforcement), the socialised costs passed through in network charges to consumers, reduce. However, during consultation stakeholders reported that they would welcome greater clarity in the regulations. Government therefore proposes to take this opportunity to clarify that the Second Comer Regime should be applied in all these instances.

#### *Legislative changes required*

26. In 2015, Government took powers through the Infrastructure Act 2015<sup>4</sup> to enable it to bring ICPs, connections between distribution systems and Section 22 agreements within scope of the regime, through amendment to secondary legislation. The primary legislation already provided the power to specify in secondary legislation, the time period to which the rules apply. In order to bring these into effect the Electricity Connection Charges Regulations 2002 (ECCR) need to be revised. A Regulatory Triage Assessment<sup>5</sup> was provided at the time, with Annex 2 outlining the main differences in the analysis between the two assessments. Without further legislation, none of the changes described above would be able to be brought into effect.

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<sup>3</sup> The costs of reinforcement are normally apportioned between the connecting customer and the DNO. This means that the connecting customer only pays for a proportionate share of the reinforcement costs that are required to accommodate its connection.

<sup>4</sup> [http://www.legislation.gov.uk/ukpga/2015/7/pdfs/ukpga\\_20150007\\_en.pdf](http://www.legislation.gov.uk/ukpga/2015/7/pdfs/ukpga_20150007_en.pdf)

<sup>5</sup> [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/388480/Regulatory\\_Triage\\_Assessment\\_Bringing\\_ICPs\\_within\\_scope\\_of\\_ECCR.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/388480/Regulatory_Triage_Assessment_Bringing_ICPs_within_scope_of_ECCR.pdf)



## Policy objectives and intended effects

27. The two key policy objectives of widening the scope and application of the Second Comer Regime are:

- To **support competition in the connections market**, by helping to ensure greater parity between DNOs/ IDNOs and ICPs. Government believes competition in connections can play a valuable role in giving customer greater choice and helping to drive up performance across the network industry (e.g. improved customer service). Making this change also signals Government's support for small and medium sized enterprises (SMEs) in this area as ICPs tend to be smaller players in the market compared to the dominant DNOs that are large monopoly providers.
- To ensure **fairer sharing of costs between parties**, by a) including customers who choose an ICP connection, a Section 22 agreement connection, or choose a connection between distribution systems and b) by extending the time period in which reimbursements apply. Second comers should have to pay for the capacity they are using of a connection that was paid for by an earlier connectee, regardless of who provided that connection and should not be allowed to 'free-ride' on infrastructure paid for by others.

## Policy options considered, including alternatives to regulation

28. Two options have been considered:

- **Do Nothing:** Continue with current position of the Second Comer Regime.
- **Policy Option:** Government to extend and update the scope and application of the Second Comer Regime by: bringing ICP-built connections, connections between distribution systems and connections using a Section 22 agreement, within scope; and extend the time limit to 10 years.

29. Widening the scope and scale of the Second Comer Regime cannot be achieved through other means, for example, voluntary agreements as network operators need a legal basis to apply second comer charges. The only alternative would be to continue with the status-quo that would perpetuate the current inequality between providers.

## Monetised and non-monetised costs and benefits of each option

### 'Do Nothing'

30. Under 'Do Nothing' the status quo continues and ICPs, connections between distribution systems and connections using a Section 22 agreement will not be brought within scope of the Second Comer Regime. Also, second comer payments on DNO-/IDNO-built connections would only be made within five years of the original connection, i.e. initial connectees are not reimbursed fairly when second comer connections are made after five years.

31. There continue to be zero costs (in terms of second comer payments) for second comers that connect to ICP-built connections, connections using a Section 22 agreement, connections between distribution systems and those second comers on DNO-/IDNO-built connections that connect between five and 10 years of the initial connection.

32. There continues to be no benefits for initial connectees that chose an ICP to provide their connection, used a Section 22 agreement or a connection between distribution systems as they will not be reimbursed by any second comers. There would continue to only be a benefit for initial connectees that chose a DNO-/IDNO-built connections up to five years after the initial connection. The DNO would continue to receive second comer payments

with respect to wider reinforcement in the vast majority of cases<sup>6</sup>, but only up to five years after the initial connection that triggered the reinforcement and only if the DNO/ IDNO provided the initial connection.

33. ICPs will remain at a potential competitive disadvantage, as if a customer opts to use them to provide their connection, the customer will not be eligible for any potential future second comer payments. It is not possible to quantify the potential competitive disadvantage as the decision to use an ICP will be informed by a range of factors, including businesses' financial situation and the wider economic situation at the time.
34. Under 'Do Nothing', the DNO will not incur any additional administration costs in terms of processing second comer payments. It will only face the administration costs associated with processing Second Comer payments on DNO-/IDNO-built connections up to five years after the initial connection was made, where the connection was made through a Section 16 process and not on a link between distribution systems.
35. Overall we think the scale of the problem under 'Do Nothing' is likely to be small due to several reasons. Firstly, there are currently relatively few payments linked to second comers on DNO-/IDNO-built connections, suggesting that under the 'Policy Option' the incidence would still be low because in most cases the capacity of the infrastructure installed is tailored to the customers demand extra capacity is only installed when standard sizes of cables and sub-stations are higher than demand needed. Secondly, the size of current second comer payments is small. Thirdly, there are relatively few connections with a Section 22 Agreement and between distribution systems. Furthermore, there are a range of other factors that determine whether a customer wishes to use an ICP, a connection between distribution systems or a Section 22 agreement (e.g. awareness, cost, reliability), resulting in lack of Second Comer payments rarely being the deciding factor.
36. However, whilst we do not think this inequity is always a *determining* factor for customer when deciding which route to take for their connections, stakeholders have reported that they have considered it and that it has been a *contributing* factor. Therefore, in line with Government's objective to support competition in the connections market and commitment to ensure fairness in the distribution of connection costs, the regime should be extended to increase the possibility of cost-sharing and help level the playing-field for independent providers. There has been broad support from stakeholders, including developers, ICPs and DNOs, for widening the scope and scale of the regime and that in this regard, the current legislation is out of date.
37. Table 1 outlines what is currently in and out of scope of the Second Comer Regime.

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<sup>6</sup> In some instances, due to a perceived lack of clarity in the legislation, DNOs might not receive a second comer payment to compensate them for their wider reinforcement. This means more costs might be passed through to consumer bills. There is no quantitative data available on this area, but based on stakeholder feedback these instances are very limited and we have therefore not monetised this.

**Table 1: Current second comer regime under ‘Do Nothing’**

Initial connection	Second comer connection occurs between 0 and five years after the initial connection is made.		Second comer connection occurs between five and 10 years after the initial connection is made.	
	Second Comer payment between connecting customers	Second comer payment between second comer and DNO (for wider reinforcement)	Second Comer payment between connecting customers	Second comer payment between second comer and DNO (for wider reinforcement)
DNO-/IDNO-built connection	✓	✓	✗	✗
ICP-built connection	✗	✗	✗	✗
Connection between distribution systems	✗	✗	✗	✗
Section 22 agreement connection	✗	✗	✗	✗

**‘Policy Option’**

38. Table 2 shows the second comer regime under the proposed ‘Policy Option’.

**Table 2: Proposed second comer regime under ‘Policy Option’**

Initial connection	Second comer connection occurs between 0 and five years after the initial connection is made.		Second comer connection occurs between five and 10 years after the initial connection is made.	
	Second Comer payment between connecting customers	Second comer payment between second comer and DNO (for wider reinforcement)	Second Comer payments between connecting customers	Second Comer payment between second comer and DNO (for wider reinforcement)
DNO-/IDNO-built connection	✓	✓	✓	✓
ICP-built connection	✓	✓	✓	✓
Connection between distribution systems	✓	✓	✓	✓
Section 22 agreement connection	✓	✓	✓	✓

39. Table 3 below sets out the additional costs and benefits we have identified with regards to the ‘Policy Option’ compared with ‘Do Nothing’.

**Table 3: Identified costs and benefits (bold rows have been quantified)**

	Costs	Benefits
<b>1. Initial connectee</b>		
<b>Initial connectee on a DNO-/IDNO-built connection</b>	<ul style="list-style-type: none"> <li>Charged for DNO/ IDNO admin (DNO/ IDNO pass through) for processing additional second comer payments <u>between five to 10 years</u> after the initial connection</li> </ul>	<ul style="list-style-type: none"> <li>Receives second comer payment <u>between five to 10 years</u> after the initial connection (transfer)</li> </ul>
<b>Initial connectee on an ICP-built connection</b> , a connection between distribution systems or a Section 22 Agreement	<ul style="list-style-type: none"> <li>Charged for DNO/ IDNO admin costs (DNO/ IDNO pass through) for processing additional second comer payments <u>within 10 years</u> of the initial connection</li> </ul>	<ul style="list-style-type: none"> <li>Receives second comer payment <u>within 10 years</u> of the initial connection (transfer)</li> </ul>
<b>2. Second comer</b>		
<b>Second comer on a DNO-/IDNO-built connection</b>	<ul style="list-style-type: none"> <li>Reimburses initial connectee and the DNO/ IDNO (for wider reinforcement)<sup>7</sup> <u>between five to 10 years</u> after the initial connection (transfer)</li> </ul>	
<b>Second comer on an ICP-built connection</b> , a connection between distribution systems or a Section 22 Agreement	<ul style="list-style-type: none"> <li>Reimburses initial connectee and DNO/ IDNO (for wider reinforcement)<sup>9</sup> <u>within 10 years</u> of the initial connection (transfer)</li> </ul>	
<b>3. DNO/ IDNO</b>		
<b>For second comers on DNO-/IDNO-built connections</b>	<ul style="list-style-type: none"> <li>DNO/ IDNO incurs admin costs for processing additional second comer payments <u>between five to 10 years</u> after the initial connection (direct cost, passed through to initial connectees)</li> </ul>	<ul style="list-style-type: none"> <li>DNO receives second comer payment <u>between five to 10 years</u> after the initial connection for wider reinforcement (direct benefit but passed through to consumers).</li> </ul>
<b>For second comers on an ICP-built connection</b> , a connection between distribution systems or a Section 22 Agreement	<ul style="list-style-type: none"> <li>DNO/ IDNO incurs admin costs for processing additional second comer payments <u>within 10 years of the initial connection</u> (direct cost, passed through to initial connectees)</li> </ul>	<ul style="list-style-type: none"> <li>DNO receives second comer payment <u>within 10 years</u> of the initial connection for wider reinforcement</li> </ul>
DNO/ IDNO	Potential loss of market share (transfer)	
4. Suppliers/Generators		<ul style="list-style-type: none"> <li>Lower distribution network charges (DNO/ IDNO pass through)</li> </ul>
5. End-consumers (including all connecting customers)		<ul style="list-style-type: none"> <li>Lower distribution network charges (Supplier pass through)</li> <li>Lower electricity prices (Generator pass through)</li> <li>Competition/equity benefits</li> </ul>
6. ICPs		<ul style="list-style-type: none"> <li>Potential gain in market share (transfer)</li> <li>Equity ('level playing field') benefit</li> </ul>
<b>7. Ofgem</b>	<ul style="list-style-type: none"> <li>Potential increase in appeals (determination) related to Second Comer payments</li> </ul>	

<sup>7</sup> Note that by clarifying the application of the Second Comer Regime with respect to DNO wider reinforcement costs, there could be slightly more transfers under the 'Policy Option'. However, as payments already happen in most cases, this is likely to be immaterial and has not been quantified.

41. The following sets out the additional costs and benefits that are anticipated from the policy change.

### **Monetised Costs**

42. Table 4 outlines the monetised (best estimate) costs associated with the 'Policy Option' in this Impact Assessment. Information on the underlying data is outlined in Annex 1. The additional annual cost associated with these additional second comers is estimated to be £1.75m (cost, 2014 prices), with a present value over a default 10 year time period of £14.54m (cost, 2014 price, discounted to 2015). All costs are individually discussed below the table.

**Table 4: Table outlining the monetised costs in terms of Annual Equivalent and NPV**

	<b>Costs</b>	<b>Annual Equivalent (2014 prices)</b>	<b>Present Value (PV) (2014 prices, discounted to 2015)</b>
<b>1. Initial connectee (pass through from DNO/ IDNO)</b>		£0.06m	£0.48m
<b>2. Second comer</b>		<b>£1.69m</b>	<b>£14.06m</b>
Second comer on a DNO-/IDNO-built connection	<ul style="list-style-type: none"> <li>Reimburses initial connectee and DNO (for wider reinforcement)<sup>9</sup> <u>between five to 10 years</u> after the initial connection (transfer)</li> </ul>	£1.14m	£9.45m
Second comer on ICP-built connection	<ul style="list-style-type: none"> <li>Reimburses initial connectee and DNO (for wider reinforcement)<sup>9</sup> <u>within 10 years</u> of the initial connection (transfer)</li> </ul>	£0.55m	£4.61m
<b>3. DNO (passed through to initial connectee)</b>		<b>£0.06m</b>	<b>£0.48m</b>
Second comer on a DNO-/IDNO-built connection	<ul style="list-style-type: none"> <li>Incurs admin costs for processing additional second comers between year five and 10 after the initial connection<sup>8</sup> (passed through to initial connectees)</li> </ul>	£0.02m	£0.19m
Second comer on ICP-built connection	<ul style="list-style-type: none"> <li>Incurs admin costs for processing second comers within 10 years after the initial connection<sup>10</sup> (passed through to initial connectees)</li> </ul>	£0.03m	£0.29m
<b>7. Ofgem (accounted for as direct cost to SO/DNO/ GDNs)</b>		£0.000m	£0.001m
	<ul style="list-style-type: none"> <li>Incurs appeal costs if customers are unhappy with the price charged</li> </ul>		
<b>TOTAL</b>		<b>£1.75m</b>	<b>£14.54m</b>

*Note:* Figures are rounded. Table includes both the widening of the scope and application of the scheme and the time limit extension. The initial connectee costs noted in row 1 (£0.06m) and DNO costs noted in row 3 (£0.06m) relate to the same cost; these are direct costs to the DNO, but they are passed on to initial connectees.

#### **1. Additional costs to the initial connectee**

- There are no direct monetised costs to initial connectees. However, DNOs recover their administration costs from the initial connectees by deducting these from the second comer payments the initial connectee receives. These are estimated to have an annual cost of £0.06m (cost, 2014 prices). These costs are accounted for as direct costs in the DNO section.

<sup>8</sup> The direct cost is to the DNO, the administrative cost will then be passed onto initial connectees via a reduced second comer payment. This is a secondary effect.

## **2. Additional costs to second comers**

### Second comer on a DNO-/IDNO-built connection

- There are additional costs for second comers that connect to DNO/ IDNO-built connections between five and 10 years after the initial connection being made. Second comers will have to pay the initial connectee (and where wider reinforcement has been required, the DNO) a second comer payment. Second comers that connect to a DNO/ IDNO-built connection within five years of it being built already pay a second comer payment to the initial connectee and the DNO (for wider reinforcement) and are not included in the additional costs.
- The analysis assumes that over the 10 year appraisal period, a total of around 1,030 second comer payments to the initial connectee and the DNO (for wider reinforcement) are made in the five to 10 years after the initial connection. This implies an additional total annual reimbursement of £1.14m (cost, 2014 prices) to initial connectees and DNOs. The present value of these costs over a default 10 year timeframe is £9.45m (cost, 2014 prices, discounted to 2015). This represents a transfer from second comers to first comers and DNOs (for wider reinforcement) five to 10 years after initial connection. The transfer to DNOs is expected to result in a reduction in network charges passed through to suppliers and, in turn, consumers (see section on monetised benefits for consumers).

### Second comer on ICP-built connection

- There are additional costs for second comers that connect to ICP-built connections within 10 years of the initial connection being made. Second comers will have to pay the initial connectee (and where wider reinforcement was required, the DNO) a second comer payment. The analysis assumes that over the 10 year appraisal period, 503 second comer payments are made within 10 years of the initial connection to initial connectees and DNOs (for wider reinforcement). This implies an additional total annual reimbursement of £0.55m (cost, 2014 prices). The present value of these costs over a default 10 year timeframe is £4.61m (cost, 2014 prices, discounted to 2015). This represents a transfer from second comers to first comers and DNOs (for wider reinforcement) within 10 years of the initial connection. The transfer to DNOs is expected to result in a reduction in network charges passed through to suppliers and, in turn, to consumers (see section on monetised benefits for consumers).

## **3. Additional costs to the DNO/ IDNOs**

- There are additional administrative costs for DNOs/ IDNOs associated with processing second comer payments. These are considered to be direct costs to DNOs/ IDNOs; however they pass these costs onto initial connectees (who may or may not be a business) by deducting them from the second comer payment.
- In order to bring ICP connections within scope, DNOs/ IDNOs need to be able to process second comer transfers between the different parties involved. To be able to do this DNOs/ IDNOs will be allowed to estimate the cost of the initial connection, as unlike where a DNO/ IDNO provided the initial connection, they will not have access to the detailed cost information where the connection was made by an independent provider. Rather than require ICPs to share commercially sensitive pricing data, the DNOs/ IDNOs should be allowed to estimate these costs based on what the costs would have been had the DNO made the connection and the change in prices since the connection was made. ICPs already routinely provide to the DNO/ IDNO the technical details of the connection as part of the 'adoption process', whereby the DNO takes ownership of the asset, so they will have the information required to estimate a proxy cost.

- These costs are incurred on processing payments and completed connection invoices. DNOs/ IDNOs will also have an administrative cost associated with processing any second comer payment, which is assumed to be £225 (cost, 2014 prices) per any completed connection invoice. In addition, DNOs/ IDNOs will have administrative costs associated with undertaking a proxy *estimate* of the costs when the initial customer connected through an ICP. Through discussions with DNOs we assume the cost incurred to estimate a cost of connection will be £1,000 (cost, 2014 prices) (see further detail in the 'Assumptions' section). This results in an annual cost impact on DNOs/ IDNOs of £0.06m (cost, 2014 prices). The present value of these costs over a default 10 year timeframe is £0.48m (cost, 2014 prices, discounted to 2015). Annex 1 sets out the data used in these calculations.

#### *4, 5, and 6. Additional costs to suppliers/generators, end-consumers and ICPs*

- There are no additional monetised costs for suppliers/generators, end-consumers, ICPs or Ofgem.

#### **7. Additional costs for Ofgem**

- Whilst DNOs are responsible for administering the process, Ofgem (the independent network regulator) act as the final arbitration point if customers are unhappy with the price charged for a connection (or reinforcement), this can include any second comer element of the connection cost. By extending the scope of the scheme, the instances of customers appealing to Ofgem against a second comer charge, could increase. Ofgem advises that there has only been one appeal in relation to Second Comer payments since the 2002 Regulations. This appeal has cost Ofgem around £1,100 (cost, 2014/15 prices). Annualising this over a 13 year time period results in £84 per year (cost, 2014/15 prices). This cost is related to the incidence of second comer payments under 'Do Nothing', i.e. around 100 second comer payments (64 on metered and 39 on unmetered connections). Under the 'Policy Option', the IA assumes there are 150 additional second comer payments (around 100 additional on DNO/IDNO-built connections due to the time limit extension and 50 on ICP-built connections). If costs are linear, this implies there could be up to £125 (cost, 2014/15 prices) additional appeal costs per year. This results in an additional cost over a 10 year time period of £1,000 (cost, 2014/15 prices, discounted to 2014).
- As Ofgem is industry-funded, these are considered to be direct costs to the System Operator (SO)/ electricity distribution network operators (DNO)/ gas distribution networks (GDN), which are then assumed to pass these costs through to generators/ suppliers and ultimately end-consumers<sup>9</sup>.

### **Non-Monetised Costs**

#### **1. Additional costs to the initial connectee**

- There are no non-monetised costs to initial connectees.

#### **2. Additional costs to second comers**

##### **Second comer on a connection between distribution systems**

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<sup>9</sup> Ofgem costs are passed on to the network businesses that hold licences for gas transportation and electricity transmission with system operator conditions (National Grid Electricity Transmission), and electricity and gas distribution. These costs are treated as 'pass-through costs', which means that licence holders, in turn, recover the costs from generators and suppliers, which ultimately pass costs onto consumers.

- There are additional costs for second comers that connect to connections between distribution systems within 10 years of the initial connection being made. Second comers will have to pay the initial connectee (and where wider reinforcement has been required, the DNO) a second comer payment. There is no quantitative evidence on how many connections between distribution systems there are (Ofgem's dataset does not provide this detail), but we are informed through consultation that they are very rare. Due to this lack of data and the small scale we have not quantified this.
- Costs to second comers that connect to connections between distribution systems represent a transfer from second comers to first comers and DNOs (for wider reinforcement) within 10 years from the initial connection. The transfer to DNO is expected to result in a reduction in network charges to consumers (see section on monetised benefits for consumers).

#### Second comer on Section 22 Agreement connection

- There are additional costs for second comers that connect to connections that used a Section 22 Agreement within 10 years of the initial connection being made. Second comers will have to pay the initial connectee (and where wider reinforcement has been required, the DNO) a second comer payment. There is no quantitative evidence on how many Section 22 agreements there are (Ofgem does not collect this data, but will start collecting this data under the RIIO-ED1 price control), but we are informed through consultation that they are very rare (e.g. one or two a year); the chances of a second comer payment therefore becoming due are remote. Due to this lack of data and the small scale we have not quantified this.
- Costs to second comers that connect to connections that used a Section 22 Agreement represent a transfer from second comers to first comers and DNOs (for wider reinforcement) within 10 years from the initial connection. The transfer to DNO is expected to result in a reduction in network charges to consumers (see section on monetised benefits for consumers).

#### Clarifying the application of the Second Comer Regime with respect to DNO incurred costs

- There are potential additional costs to second comers if, by clarifying the legal framework, a greater number of second comer payments are made to the DNO in respect to wider reinforcement (as set out in footnote 5). There is no data on this area, but DNOs report that they already apply the Second Comer Regime in the vast majority of cases, so we expect these additional costs to be small, both in terms of transfers and administrative costs, therefore this has not been quantified.

### **3. Additional costs to the DNO/ IDNO**

- The 'Policy Option' aims to support competition in the connections market, by ensuring parity between different connection providers in terms of their status under the Second Comer Regime. Whilst we do not think that the inequity under 'Do Nothing' is always a *determining* factor for customer when deciding who to use to provide a connection, some stakeholders have reported that they have considered it and that it has been a *contributing* factor. Therefore, there could be a small negative impact on the market share of DNOs/ IDNOs, but in the absence of any meaningful data here, we have not quantified this cost.
- We do not expect any other costs, including any new familiarisation costs for DNOs. DNOs are already calculating and processing second comer payments in relation to DNO connections and, under the policy proposal, ICPs will not need to pass any more information than they currently already have to under existing processes. While



estimating ICP costs will be a new process for DNOs, this is deemed to be straightforward as it requires using new information but existing methods.

*4, 5, 6 and 7. Additional costs for suppliers/generators, end-consumers, ICPs and Ofgem*

- There are no additional non-monetised costs for suppliers/generators, end-consumers, ICPs (ICPs already provide the information required to administer the scheme, as part of the existing adoption process where connections are transferred to the DNO/ IDNO) or Ofgem.

**Monetised benefits**

43. Table 5 outlines the monetised (best estimate) benefits associated with the 'Policy Option' in this Impact Assessment. Information on the underlying data is outlined in Annex 1. The additional annual benefit associated with these additional second comers is estimated to be £1.69m (benefit, 2014 prices), with a present value over a default 10 year time period of £14.06m (benefit, 2014 price, discounted to 2015). All benefits are individually discussed below the table.

**Table 5: Breakdown of monetised benefits**

	<b>Benefits</b>	<b>Annual Equivalent (2014 prices)</b>	<b>Present Value (PV) (2014 prices, discounted to 2015)</b>
<b>1. Initial connectees</b>		<b>£0.24m</b>	<b>£1.97m</b>
Initial connectee with a DNO-/IDNO-built connection	<ul style="list-style-type: none"> <li>• Receives second comer payment between <u>five to 10 years</u> after the initial connection (transfer)</li> </ul>	£0.16m	£1.33m
Initial connectee with ICP-built connection	<ul style="list-style-type: none"> <li>• Receives second comer payment <u>within 10 years</u> of the initial connection (transfer)</li> </ul>	£0.08m	£0.65m
<b>2. Second comer</b>		-	-
<b>3. DNO (passed through to consumers)</b>		<b>£1.45m</b>	<b>£12.09m</b>
Second comer on a DNO-/IDNO-built connection	<ul style="list-style-type: none"> <li>• Receives second comer payment between <u>five to 10 years</u> after the initial connection (for wider reinforcement)<sup>9</sup></li> </ul>	£0.98m	£8.12m
Second comer on ICP-built connection	<ul style="list-style-type: none"> <li>• Receives second comer payment <u>within 10 years</u> of the initial connection (for wider reinforcement)<sup>9</sup></li> </ul>	£0.48m	£3.96m
<b>TOTAL</b>		<b>£1.69m</b>	<b>£14.06m</b>

Note: Figures are rounded. Table includes both the widening of the scope and application of the scheme and the time limit extension.

**1. Additional benefit to the initial connectee**

**Initial connectee with a DNO-/IDNO-built connection**

- By extending the time limit from five to 10 years, there are additional second comer payments made to initial connectees that chose a DNO or IDNO for their connection. The analysis assumes that over the 10 year appraisal period, 479 additional second comer payments are made to initial connectees (payments to the DNO for wider reinforcement are captured in the DNO section) between five to 10 years after the initial connection. Initial connectees that use a DNO or IDNO are estimated to receive a total additional annual reimbursement of £0.16m (benefit, 2014 prices) from second

comers beyond year five. The present value of these benefits over a default 10 year timeframe is £1.33m (benefit, 2014 prices, discounted to 2015). This represents a transfer from second comers to first comers.

- The initial connectee will not receive all of these benefits as the administration costs to DNOs (the entities that process the second comer payments) will be deducted by the DNO from the second comer payment transfer to the initial connectee. These administration costs are estimated to have an annual impact of £0.06m (cost, 2014 prices). These have been captured in the 'Additional costs to DNOs' section above. This is considered a secondary pass through impact and is only mentioned here for information.

#### Initial connectee with ICP-built connection

- There are additional reimbursements for initial connectees where an ICP provided the initial connection. The analysis assumes that over the 10 year appraisal period, 234 second comer payments are made to initial connectees within 10 years of the initial connection (payments to the DNO for wider reinforcement are captured in the DNO section). By including ICPs within the second comer regime, initial connectees that use an ICP are estimated to receive a total annual reimbursement of £0.08m (benefit, 2014 prices) from second comers. The present value of these benefits over a default 10 year timeframe is £0.65m (benefit, 2014 prices, discounted to 2015). This represents a transfer from second comers to first comers.

#### **2. Additional benefit to the second comer**

- There are no monetised benefits to second comers.

#### **3. Additional benefits to the DNO**

##### Benefit to the DNO from second comers on DNO/ IDNO built connections

- Where wider reinforcement was required at the time of the initial connection, DNOs will receive additional reimbursements.<sup>9</sup> The analysis assumes that over the 10 year appraisal period, due to the time limit extension from five to 10 years, DNOs will, under the 'Policy Option', be reimbursed for wider reinforcement that happened at the time of the initial connection for longer. The analysis assumes there are 552 additional second comer payments over a 10 year time period. DNOs are estimated to receive a total additional annual reimbursement of £0.98m (benefit, 2014 prices) from second comers five to 10 years after the initial connection was made. The present value of these benefits over a default 10 year timeframe is £8.12m (benefit, 2014 prices, discounted to 2015). As the DNO will be reimbursed for the additional reinforcement, these benefits are expected to be passed onto suppliers and, in turn, consumers via a reduction in network charges (see section on monetised benefits for consumers).

##### Benefit to the DNO from second comers on an ICP-built connection

- Where wider reinforcement was required at the time of the initial connection, DNOs will receive additional reimbursements.<sup>9</sup> The analysis assumes that over the 10 year appraisal period, as a result of including ICP-built connections within the legislation (and the time limit extension from five to 10 years), DNOs will, under the 'Policy Option', be reimbursed for wider reinforcement that happened at the time of the initial connection that used an ICP. The analysis assumes there are 269 additional second comer payments over a 10 year time period. DNOs are estimated to receive a total additional annual reimbursement of £0.48m (benefit, 2014 prices) from second comers within 10 years after the initial connection was made. The present value of these benefits over a default 10 year timeframe is £3.96m (benefit, 2014 prices,

discounted to 2015). As the DNO will be reimbursed for the additional reinforcement, these benefits are expected to be passed onto suppliers and, in turn, consumers via a reduction in network charges (see section on monetised benefits for consumers).

#### **4 and 5. Additional benefits to suppliers/generators and end-consumers**

- The DNO is expected to pass on its additional annual reimbursements of £0.95m to suppliers and generators, which, in turn, pass these on to end-consumers via a reduction in network charges and electricity prices, respectively. The additional reimbursements are considered to be direct benefits to DNOs and are accounted for as such in this IA. The benefit for suppliers/generators and ultimately end-consumers is considered to be secondary and only mentioned here for information.

#### **6 and 7. Additional benefits to ICPs and Ofgem**

- There are no monetised benefits for ICPs or Ofgem.

### **Non-monetised benefits**

#### **0. Additional benefit to the initial connectee**

##### **Initial connectee with a connection between distribution systems**

- There are additional second comer payments to initial connectees where the initial connection was a connection between distribution systems and the second comer connected within 10 years of the initial connection. This represents a transfer from second comers to first comers. The Ofgem dataset does not hold specific information on the number of these types of connections. Feedback from stakeholders suggests that this is likely to be low and negligible.

##### **Initial connectee with a Section 22 Agreement connection**

- There are additional second comer payments to initial connectees where the initial connection was undertaken under a Section 22 agreement and the second comer connected within 10 years of the initial connection. This represents a transfer from second comers to first comers and DNOs. As section 22 agreements are private agreements between connectees and the DNO, we do not have any information on the number of section 22 agreements. Feedback from stakeholders suggests that this is likely to be low and negligible.

##### **All initial connectees**

- All initial connectees will benefit from the 'Policy Option' as by improving the level playing field across connection providers and by extending the time limit, connecting customers can better and for longer harness the benefits of competition, i.e. by choosing the most competitive provider in the market and being able to receive second comer payments no matter which provider was chosen. Government believes competition in connections can play a valuable role in giving customers greater choice and helping to drive up performance across the network industry (e.g. improved customer service).

#### **2. Additional benefit to the second comer**

- There are no non-monetised benefits to second comers.

#### **3. Additional benefits to the DNO**

- There are additional second comer payments to DNOs within 10 years from the initial connection for wider reinforcement if the initial connection was a connection between

distribution systems or based on a Section 22 Agreement. This represents a transfer from second comers to the DNO. The Ofgem dataset does not hold specific information on the number of these types of connections. Feedback from stakeholders suggests that this is likely to be low and negligible.

- The additional second comer payments that DNOs receive under the 'Policy Option' are expected to be passed through to suppliers, which, in turn, pass these on to network consumers via lower network charges.
- There are potential additional costs to second comers if, by clarifying the legal framework, a greater number of second comer payments are made to the DNO in respect to wider reinforcement (as set out in footnote 5). There is no data on this area, but DNOs/ IDNOs report that they already apply the Second Comer Regime in the vast majority of cases, so we expect these additional costs to be small, both in terms of transfers and administrative costs, therefore this has not been quantified.

#### **4 and 5. Additional benefits to suppliers/generators and end-consumers**

- The 'Policy Option' ensures that those using network reinforcements paid for by the DNO are paying their fair share up to 10 years after the initial connection, which helps to reduce the socialised costs passed on to suppliers/generators, which, in turn, pass these on to end-consumers in the form of lower network charges and electricity prices, respectively (see section on monetised benefits for end-consumers).
- More generally, (as already mentioned above under 'initial connectees', all connecting customers will benefit from the 'Policy Option' as by improving the level playing field across connection providers, connecting customers can better harness the benefits of competition, i.e. by choosing the most competitive provider in the market and being able to receive second comer payments no matter which provider was chosen. Government believes competition in connections can play a valuable role in giving customers greater choice and helping to drive up performance across the network industry (e.g. improved customer service).

#### **6. Additional benefits to ICPs**

- Bringing ICPs within scope should help support competition and equity in the connections market, as it removes a barrier that may deter customers from using them. This is beneficial for ICPs who tend to be smaller players in the market (e.g. SMEs) compared to the dominant DNOs that are larger traditional monopoly providers in the connections market in their franchise areas, but also customers more generally. Customers can benefit from healthier competition in the connections market, helping to increase choice and drive up performance across the industry (e.g. improved customer service). It is not possible to quantify this benefit.
- Overall we think it is likely to be small due to several reasons. Firstly, the number of second comer payments is currently low. Secondly, some customers are not aware of the second comer regime and where customers are aware, it is not always considered 'bankable'. Thirdly, there is a range of other factors that determine whether a customer wishes to use an ICP (e.g. awareness, cost, reliability). Some stakeholders have reported, however, that it is a factor they consider when deciding whether to use an ICP or not.

#### **7. Additional benefits to Ofgem**

- There are no additional non-monetised benefits for Ofgem.

### **Summary**

44. The monetised (best estimate) total annual cost to society is £1.75m (cost, 2014 prices) while the monetised (best estimate) total annual benefit to society is £1.69m (benefit, 2014 prices). This results in a net annual cost to society of £0.06m (cost, 2014 prices). The NPV over a default 10 year timeframe is -£0.48m (net benefit, 2014 prices, discounted to 2015).
45. This monetised NPV does not cover all of the costs and benefits associated with the 'Policy Option'. Most importantly, it was not possible to quantify the benefits associated with likely improvements in *economic efficiency* due to more competition or the likely improvements in *equity* due to promoting fairer cost sharing between all parties and for a longer time period. These benefits would improve the NPV of the 'Policy Option'. However, it is uncertain how large these benefits would be as the current inequity between different connection providers under the Second Comer Regime is generally unlikely to be a *determining factor* for a customer when deciding to use an ICP or DNO to provide a connection, but some stakeholders have reported that it has been a *contributing factor*.
46. The monetised NPV also does not include the impact of introducing connections between distribution systems, Section 22 agreements and clarifying the application of the Second Comer regime with respect to DNO incurred wider reinforcement costs is likely to have a negligible impact on the NPV.
47. Whilst we estimate the non-monetised benefits of the proposed change will be relatively low for the reasons outlined above, we do think the change should be made. The omission of ICP is now an anomaly and a result of competition bedding down after the original legislation was drafted. Given that this could create barriers to entry and expansion for ICPs, customers that use an ICP, a connection between distribution systems, or a Section 22 agreement should be made eligible for second comer payments and therewith be put on a more equal footing with DNOs in respect of second comers.
48. Clarifying the legislation around second comers onto reinforced networks will ensure that consumers in all DNOs are treated fairly (although this is already happening in the vast majority of cases).
49. In line with Government's objective to support competition in the connections market, we believe the regime should be updated to level the playing-field. There has been unanimous support from stakeholders, including developers, ICPs and DNOs, for widening the scope and application of the second comer regime.

### **Assumptions and Risks**

50. This section sets out which data sources we have used and which assumptions we have made in order to assess the costs and benefits associated with making the proposed changes.

#### **Number of connections and second comers**

51. To establish the number of connections and second comer payments this IA uses data collected by Ofgem since 2010/11 through the annual DNO reporting cycle (*The Connections Reporting Pack*). This dataset provides information on the number of connections, including the number of metered 'connection projects' and unmetered 'end consumer or exit point connections'; the number of second comer payments (for metered connections only); and respective market-shares of the connections market held by DNOs, IDNOs and ICPs.
52. Receiving a longer time series, i.e. with data prior to 2010/11 is difficult. DNOs reported that it would be very resource intensive to provide figures for a longer timeframe.

However, they have reported that they believe the number of payments has remained broadly flat over the years.

53. The Ofgem dataset does not hold information on the potential number of second comer payments that would be due on ICP-built connections, on connections between distribution systems, on connections with a Section 22 Agreement, or on second comers between year five and 10 after the initial connection on DNO-/IDNO-built connections under the 'Policy Option'. The dataset also does not hold information on the number of second comers in relation to unmetered connections. To address these issues this IA makes the following assumptions:

- Second comers on ICP-built connections: To derive an estimate of second comers on ICP-built metered connections (see treatment of unmetered connections below), we have applied the proportion of second comer metered connections and payments for DNO connections as reported in the *Connections Reporting Pack*. There is a risk that this may not be the case due to the differences between ICP- and DNO-/IDNO-built connections. To address this risk we have undertaken sensitivity analysis (see below).
- Second comers on connections between distribution systems: We do not have any data on the number of metered or unmetered connections between distribution systems as these are not separately listed in Ofgem's *Connections Reporting Pack*. Ofgem have stated that the number of connections between distribution systems a year is low. Given how few second comer connections there are per DNO or IDNO connection, the impact of bringing in connections between distribution systems is likely to be negligible.
- Second comers on Section 22 agreement connections: We do not have any data on the number of metered or unmetered section 22 agreements as these are private agreements between those who do the connections, therefore Ofgem do not collect any data on these connections. Ofgem have stated that the number of section 22 agreements a year is low (1 or 2). Given how few second comer connections there are per DNO connection, the impact of bringing in section 22 agreements is likely to be negligible.
- Second comers on DNO-/IDNO-built connections between year five and 10 (time limit extension): We do not have data on the second comer connections that would have prompted payments if the time limit had been longer. At present, second comer payments can only be paid within five years of the initial connection being made. Therefore, using feedback from stakeholders (Ofgem, DNOs, IDNOs, ICPs and developers) gathered through a consultation, workshops and series of bilateral discussions we have made a range of informed assumptions. Broadly, stakeholders have advised that they would expect the number of second comer payments being made between years five and 10, to be at the same rate as within the first five years. Therefore the central assumption is that the overall number of second comer payments doubles. Given that we are using the proportion of second comers on DNO-/IDNO-built connections to derive the number of second comers on ICP-built connections, the analysis also doubles the number of second comers on ICP-built connections.

Sensitivity analysis has been done around this assumption due to the risk that the proportion of second comer payments between five and 10 years after the initial connection differs to the proportion seen between years 0 and five.

- Second comers on unmetered connections: Unlike metered connection data, unmetered connection information is on an 'end consumer' or 'exit point' basis. In order to make it comparable to the 'connection project' basis we are using for

metered projects, we have considered the size of the metered and unmetered markets on an 'exit point' basis (roughly similar in size) and used this information to say that the unmetered connections market on a 'project connection' basis is of similar size as the metered connections market on a 'project connection' basis. Due to competition having been more successful in unmetered connections, we would expect more second comer connections on unmetered ICP-built connections. Therefore, rather than taking the market shares as seen in the metered market, the analysis applies the market shares associated with ICPs on an exit point connection basis. To derive the number of second comers, the analysis then applies the proportion of second comer metered connections and payments for DNO/ IDNO connections as reported in the *Connections Reporting Pack* to the assumed unmetered project connections.

54. **Deterrent effect of current inequity:** We have no quantitative data on how many customers have been deterred from choosing an ICP, a Section 22 agreement or a connection between distribution systems as a result of the inequity in the application of the Second Comer Regime. We have therefore had to draw on comments and views from stakeholders e.g. developers, ICPs and DNOs, in order to assess the impact. ICPs and some developers believed there had been some contributing deterrent effect on using an ICP when this was considered; DNOs were unable to make a judgement.
55. **The size of second comer payments between parties:** The Ofgem database over 2011/12 and 2013/14 suggests that the average second comer payment to initial connectees (on DNO-/IDNO-built connections) was £3,300 (transfer, 2014 prices) and the average second comer payment to DNOs (for use of wider reinforcement) was £17,700 (transfer, 2014 prices). The analysis assumes that this would also be representative of the average second comer payments associated with other types of connections. See sensitivity analysis around these values below.
56. **The administrative cost for the DNO per second comer payment:** Evidence on the administrative costs for the DNO relies on stakeholder feedback. DNOs have told us that processing second comer payments on DNO-/IDNO-built connections incur a fixed fee (for checking eligibility and processing) of around £225 (cost, 2014 prices) per completed connection invoice. This weighted average came from a range of £100 to £250 per completed connection invoice. The IA assumes that the administration costs per second comer payment are the same five to 10 years after the initial connection was made as they were for 0 to five years after the initial connections was made. DNOs have supported this assumption. Furthermore, the IA assumes that this administration cost applies for handling transfers between developers but also transfers between the developer and the DNO (for wider reinforcement). While the costs for the latter might be lower as they do not require the same level of interaction with external parties, we have assumed a conservative/high estimate.
57. However, in relation to processing second comer payments for non-DNO-/IDNO-built connections specifically, there will be an additional administrative cost. Under the 'Policy Option', DNOs would not have access to the *actual* cost of the first comer connection where an ICP is used. The reason for this is that sharing this information would reveal commercially sensitive data to the DNO about the non-DNOs pricing approach. It may also introduce perverse incentives for a non-DNO to artificially inflate (or deflate) the cost when sharing with the DNO. During stakeholder discussion ICPs and DNOs have stated this is not a tenable option.
58. Instead, DNOs will *estimate* the cost of the initial connection based on its own costing formula and the detail of the assets installed (as the DNO is required to adopt the asset into its network, it already has this information). This can then provide a proxy cost to which base the second comer payment on. DNO stakeholders have said estimating the proxy

quote would be significantly more time consuming than dealing with a regular second comer quote (which mainly involves checking eligibility and processing). They provided a range of £800 to £1,500, with a weighted average of £1,000 (cost, 2014 prices) per quote. Using this information, the analysis assumes on average £225 (cost, 2014 prices) per completed connection invoice (for checking eligibility and processing) and a further £1,000 (cost, 2014 prices) per case where the initial connection was provided by an ICP to calculate a light-touch quote for the notional project. The latter only applies to transfers between customers, as in respect to the transfer from a second comer to a DNO, the DNO will already hold the actual cost information (as they will have done the work) so will not need to generate a proxy estimate. See sensitivity analysis around these values below.

59. **Additional appeal cost for Ofgem:** Based on Ofgem advice, this IA assumes that appeals relating to Second Comer payments have cost Ofgem around £1,100 (cost, 2014/15 prices) over the last 13 years. Annualising this results in £84 per year (cost, 2014/15 prices). This cost is related to the incidence of second comer payments under 'Do Nothing', i.e. around 100 second comer payments (64 on metered and 39 on unmetered connections). We have then linearly extrapolated this for the additional incidence of Second Comer payments under the 'Policy Option'.
60. **Connection providers being businesses:** In reality not all connections will be undertaken by businesses as some people will self-build their connections. We have no information on the proportion of connections that will be self-build versus undertaken by businesses. However, the large connections are more likely to be undertaken by businesses and therefore that is where the main transfers will take place. Due to lack of this data, we have assumed that all connections (both initial and second comer) are undertaken by businesses. Therefore, costs to businesses are likely to show an upper bound estimate.

### **Sensitivity analysis**

61. Three scenarios have been run to get the best estimate NPV, and NPVs associated with a low and high scenario. The low and high scenario use sensitivities assumptions:
- a) the average transfer amount from second comers to initial connectees and DNOs (for wider reinforcement);
  - b) the administrative cost to DNOs of undertaking a proxy estimate;
  - c) the administrative costs to DNOs of processing the second comer payment;
  - d) the amount of second comer connections beyond year five; and
  - e) the proportion of second comer connections 0 to five years from the initial connection.
- a) The medium estimate of the average transfers (used in the 'best estimate' NPV in this IA) comes as an average of the transfers that happened from second comers to initial connectees and DNOs (for wider reinforcement) between 2011/12 and 2013/14. The low assumption is the year that had the lowest average transfer (2011/12) and the high scenario has the average transfer where it was the highest (2013/14).
- b) When second comers connect to connections built by ICPs, DNOs are going to have to undertake a proxy estimate of the cost the initial connection was. The cost of a DNO undertaking a quote is estimated around £1,000 and this is taken as being proportionate for proxy estimates of connection costs. A range of £800 to £1,500 was provided by stakeholders, with £1,000 being the most suggested cost.



- c) Administration costs will differ between DNOs, so there will be no one number of how much it costs a DNO to process second comer payments. Through engagement with industry, we received a range of the administration costs for DNOs to process second comer payments. The administration costs for DNOs ranged from £100 to £250 for DNOs to process second comer payments. £225 was taken as the best estimate as responses on administration costs tended to be at the high end of the range.
- d) It is uncertain how many second comer payments will occur after the five year time limit. Views from stakeholders suggest that we would expect the same number of second comer payments between years five and 10. As there is uncertainty around those numbers we have done some sensitivity analysis. In the low scenario it is assumed that half as many second comer payments take place between years five and 10 as between years 0 and five. In the high scenario it is assumed that double as many second comer payments take place between years five and 10 as between years 0 and five.
- e) It is uncertain what the proportion of second comer connections and payments will be on ICP-built connections when they are brought within the scope and scale of the Second Comer Regime. It has been assumed that the proportion is equivalent to the average annual proportion on DNO-/IDNO-built connections. There is a risk that this may not be the case due to the differences between ICP and DNO-/IDNO-built connections. The best scenario uses the average proportion of DNO connections that are second comers between years 2011/12 and 2013/14. The high scenario uses the year that had the highest proportion of second comer connections (2013/14) and the low scenario uses the year that had the lowest proportion of second comer connections (2011/12).

**Table 6: Sensitivity analysis**

	Low	Best	High
<b>Average Second Comer Transfer</b>			
Between Second Comer and initial connectee	£2,800	£3,300	£4,000
Between second comer and DNO	£7,500	£17,700	£22,400
<b>Admin Costs</b>	£100	£225	£250
<b>Notional Quote</b>	£800	£1,000	£1,500
<b>Time Limit Extension</b>	Half as many second comer connections take place five to 10 years after the initial connection as between 0 and five years.	The same amount of second comer connections take place five to 10 years after the initial connection as between 0 and five years.	Double as many second comer connections take place five to 10 years after the initial connection as between 0 and five years.
<b>Proportion of connections that involve second comer payments.</b>	0.4%	0.13%	0.24%

62. Table 7 outlines the results of the sensitivity analysis as described above.

**Table 7: Results of Sensitivity analysis (net benefit, 2014 prices, discounted to 2015)**

	<b>Low (£m)</b>	<b>Best (£m)</b>	<b>High (£m)</b>
<b>Present Value (PV) of Costs</b>	<b>£1.39m</b>	<b>£14.54m</b>	<b>£59.25m</b>
<b>Present Value (PV) of Benefits</b>	<b>£1.31m</b>	<b>£14.06m</b>	<b>£57.79m</b>
<b>Net Present Value (NPV)</b>	<b>-£0.08m</b> (highest net benefit)	<b>-£0.48m</b>	<b>-£1.45m</b> (lowest net benefit)

Note: Figures may not sum due to rounding

## Direct costs and benefits to business calculations (following OITO methodology)

63. Amendment to the secondary legislation to widen the scope and scale of the Second Comer Regime has a direct impact on business and therefore the amendment falls within scope of the one-in, two-out (OITO) framework as it concerns the regulation of businesses and involves direct impacts on businesses. For OITO purposes the present values have been converted into a 2014 price base and have been discounted to 2015 (using a 3.5% social discount rate). Costs are considered for the OITO default 10 year period as the proposed policy change has no end date. Using the same assumptions as above, the direct costs and benefits to businesses are:

64. The **direct cost impact** of the policy change on businesses includes:

- a direct cost to second comers on DNO-/IDNO-built connections due to the additional payments they have to make to initial connectees and DNOs (for wider reinforcement) five to 10 years after the initial connection.
- a direct cost to second comers on ICP-built connections due to the additional payments they have to make to initial connectees and DNOs (for wider reinforcement) within 10 years of the initial connection.
- a direct cost to second comers on connections between distribution systems or those that have used a Section 22 Agreement; due to lack of data these have not been monetised. However, they are likely to be negligible.
- a direct cost to DNOs in the form of increased administration costs due to processing second comer payments. The pass through of these administration costs to initial connectees is classified as a second order pass through impact under OITO.
- a direct cost to the SO, DNOs and GDNs in the form of increased appeals costs that Ofgem, an industry funded regulator, passes on to these parties.

The total monetised direct cost impact is calculated to have a present value of £14.54m (2014 prices, discounted to 2015).

65. Indirect (secondary or pass through) costs include costs to DNOs/ IDNOs should they lose market share as a result of the proposed 'Policy Option'.

66. The **direct benefits impact** of the policy change on businesses includes:

- a direct benefit to initial connectees on DNO-/IDNO-built connections due to additional payments they receive from second comers that connect five to 10 years after the initial connection.
- a direct benefit to initial connectees on ICP-built connections due to the additional payments they receive from second comers within 10 years of the initial connection.
- a direct benefit to initial connectees on connections between distribution systems or those that have used a Section 22 Agreement; due to lack of data these have not been monetised. However, they are likely to be negligible.
- a direct benefit to DNOs due to the additional payments they receive from second comers that make use of reinforcements triggered by initial connectees on ICP-built connections within 10 years of the initial connection.

- a direct benefit to DNOs due to the additional payments they receive from second comers that make use of reinforcements triggered by initial connectees on DNO-/IDNO-built connections between five and 10 years of the initial connection.

The total monetised direct benefit is estimated to have a present value of £14.06m (2014 prices, discounted to 2015).

67. Indirect (secondary or pass through) benefits include benefits to suppliers/ generators and end-consumers due to potentially lower network charges and electricity prices passed through by suppliers and generators, respectively. There are further indirect benefits to consumers (including all connecting customers) from increased competition in the connections market. However, this is a behaviour change element and therefore not considered as a direct benefit for the purpose of OITO. Increased equity is considered as an indirect impact which is achieved through the redistribution of costs (direct impacts).
68. In reality not all connections will be undertaken by businesses as some people will self-build their connections. We have no information on the proportion of connections that will be self-build versus undertaken by businesses. As the large connections are more likely to be undertaken by businesses and therefore that is where the main transfers will take place, we have assumed that all connections (both initial and second comer) are undertaken by businesses.
69. The total Present Value of Net Costs to Business (PVNCB) (best estimate) is equal to £0.48m (cost, 2014 prices, discounted to 2015). Using this value, the equivalent annual net cost to business (EANCB), calculated with reference to the 'Do Nothing' option, is £56,100 (cost, 2014 prices).

$$EANCB = \frac{£0.48m}{a_{t,r}} = £56,100$$

$$\text{Where } a_{t,r} = \frac{1+3.5\%}{3.5\%} \left[ 1 - \frac{1}{(1+3.5\%)^{10}} \right]$$

## **Rationale and evidence that justify the level of analysis used in the IA (proportionality approach)**

70. The proposed change to update the scope and application of the second comer regime in the ECCR legislation does not present a contentious policy change. The principle of the Second Comer Regime was accepted at its inception and the amendments proposed are designed to correct anomalies in the current legislation. It is low risk and is likely to have a low impact. During stakeholder discussions there has been unanimous agreement for the principle of widening the scope and scale of the Second Comer Regime. There is sufficient time to analyse readily available information from Ofgem and stakeholders. However, a lot of the information especially on benefits is qualitative rather than quantitative and the scale of impacts does not justify further resource being spent on retrieving further quantitative evidence. There is also uncertainty especially around the expected benefits of the legislation change. The IA has quantified the impacts as best as possible recognising the inherent uncertainty.
71. To attempt to quantify further the costs and benefits associated with this change would be costly and time-consuming as it would involve undertaking a complex and detailed survey into the number of incidents where ICPs, IDNOs and DNOs have been used and second comers subsequently connected and customer decision-making was influenced. We do not believe this would be proportionate to the proposals being considered.
72. We have carried out extensive discussions with stakeholders including Ofgem, DNOs, ICPs and Developers there is broad support for these changes which all stakeholders believe will assist in creating a level playing field within the connections market.

## **Specific Impact Tests**

### **Competition**

73. We anticipate that by widening the scope and scale of the Second Comer Regime there will be a positive impact on competition in the connections market. We believe that by allowing other participants in the second comer market, consumers will have a greater choice between connection providers and this will lead to better service for customers. As non-DNO connection providers tend to be smaller players in the market compared to the dominant DNOs, this policy signals support for small and micro businesses (as explained below).

### **Impact on Micro-, Small and Medium Businesses**

74. As outlined above bringing other connection providers within scope of the Second Comer Regime should help support competition in the connections market. This is beneficial for ICPs who tend to be smaller players in the market (e.g. SMEs) compared to the dominant DNOs that are larger traditional monopoly providers in the connections market in their franchise areas. Importantly, it also benefits customers more generally as healthier competition in the connections market increases choice and drives up standards and performance across the industry (e.g. improved customer service). It is not possible to quantify this benefit. Overall we think it is likely to be small (for the reasons noted in the supporting evidence) but some stakeholders have reported that it is a factor they consider when deciding whether to use an ICP or not.

### **Distributional Impact**

75. As this policy will result in more second comer payments from second comers to initial connectees that they didn't do previously, there will be a distributional impact of this policy. As second comers will now be transferring money for the capacity they are using on the network, there will be a fairer distribution of costs, leading to an improvement in equity. We believe that this policy leads to a fairer distribution of cost sharing.

### **Other Impacts**

76. There will be no other impacts, including (but not limited to) the following areas:

- Human Rights Impact
- Wider Environmental impact
- Greenhouse gas impact
- Health Impact
- Rural proofing impact

## Summary and preferred option with description of implementation plan

77. Whilst we estimate the benefits of the proposed change will be relatively low for the reasons outlined above, we do think the change should be made. The omission of non-DNO connections is now an anomaly and a result of competition bedding down after the original legislation was drafted. Given that this could create barriers to entry and expansion for ICPs, customers that use a non-DNO connection should be made eligible for second comer payments and therewith be put on a more equal footing with DNOs in respect of second comers.
78. Government believes competition in connections can play a valuable role in giving customer greater choice and helping to drive up performance across the network industry (e.g. improved customer service). Making this change also signals Government's support for SMEs in this area as non-DNO connectors tend to be smaller players in the market compared to the dominant DNOs that are large monopoly providers.
79. Furthermore, whilst we do not think this inequity is always a *determining* factor for customer when deciding who to use to provide a connection, some stakeholders have reported that they have considered it and that it has been a *contributing* factor. Therefore, in line with Government's objective to support competition in the connections market, we believe the regime should be updated to level the playing-field. There has been unanimous support from stakeholders, including developers, ICPs and DNOs, widening the scope and scale of the regime.
80. The assessment of the monetised and non-monetised costs and benefits of the 'Policy Option' against 'Do Nothing' has shown that the best estimate annual cost to society is £1.75m (cost, 2014 prices) while the best estimate annual benefit to society is £1.69m (benefit, 2014 prices). This results in a net annual cost to society of £0.06m (cost, 2014 prices). The NPV over a default 10 year timeframe is -£0.48m (net benefit, 2014 prices, discounted to 2015).
81. The sensitivity analysis has shown that the annual cost to society could be as high as £7.12m (cost, 2014 prices) and the annual benefit to society could be as high as £6.95m (benefit, 2014 prices). This results in a net annual cost to society of £0.17m (cost, 2014 prices). The NPV over a default 10 year timeframe is -£1.45m (net benefit, 2014 prices, discounted to 2015). At the lower bound the annual cost to society could be as low as £0.17m (cost, 2014 prices) and the annual benefit to businesses could be as low as £0.16m (benefit, 2014 prices). This results in a net annual cost to society of £0.01m (cost, 2014 prices). The NPV over a default 10 year timeframe is -£0.08m (net benefit, 2014 prices, discounted to 2015). The quantified benefit is related to fairer sharing of costs between second comers and initial connectees and DNOs (for wider reinforcement). It is not possible to quantify fully the benefits of the proposed policy change (the above quantifies the benefit of fairer cost sharing), but we believe they will outweigh the additional administrative costs that it will bring as it will help to support competition in the connections market, by ensuring parity between different connection providers. It is also not possible to quantify the competition benefits associated with the 'Policy Option', but it is anticipated that this would result in larger benefits. The impact of introducing connections between distribution systems, Section 22 agreements and clarifying the application of the Second Comer regime with respect to DNO incurred costs is likely to have a negligible impact on the NPV.

## **Policy evaluation**

82. Ofgem is responsible for regulating distribution network operators, including ensuring the compliance with the Second Comer Regime. Since October 2010, DNOs have an obligation to report any new connections and quotes (including information on second comers and connection provider, e.g. ICP or DNO) to Ofgem. This provides data on the number and size of second comer payments on ICP-built connections and related DNO network reinforcements available. This will enable us to monitor how many ICP connections are linked to second comer payments. It will not, however, allow us to monitor the benefits for competition as these will be impacted by a range of factors (e.g. awareness, cost, reliability). In order to capture a fuller, albeit more anecdotal picture, we will also engage with stakeholders to understand the impacts on the ground.



## Annex 1 – Outline of data

### Connections Data – Central assumptions

<b>Figures from Dataset</b>	<b>Annual</b>
Average number of metered connection projects every year (2011/12-2013/14)	49,400
Average number of DNO-/IDNO-built metered connection projects every year (2011/12-2013/14)	49,200
Average number of ICP-built metered connection projects every year (2011/12-2013/14)	207
Average number of second comer payments on DNO-/IDNO-built metered connection projects every year (2011/12-2013/14)	62
Of which: Payments to initial connectees	30
Of which: Payments to DNOs (for wider reinforcement)	34
Average proportion that pays second comer payments on DNO-/IDNO-built metered connection projects every year (2011/12-2013/14)	0.13%
Of which: Proportion of payments to initial connectees	0.06%
Of which: Payments of payments to DNOs (for wider reinforcement)	0.07%
<b>Assumptions</b>	
Average number of total unmetered connection projects every year (2011/12-2013/14).	49,400
Average number of unmetered DNO-/IDNO-built connection projects every year (2011/12-2013/14)	30,200
Average number of second comer payments on DNO-/IDNO-built metered connection projects every year (2011/12-2013/14)	38
Of which: Payments to initial connectees	18
Of which: Payments to DNOs (for wider reinforcement)	21
Average number of unmetered ICP-built connection projects every year (2011/12-2013/14)	19,200
<b>Figures from calculations for the 'Policy Option'</b>	
<b>Annual</b>	
Assumed number of second comer transfers <u>between developers</u> on ICP-built metered and unmetered connection projects (with a 10 year time limit)	23
Assumed number of second comer transfers <u>between developer and DNO</u> (for wider reinforcement) on ICP- built metered and unmetered connections (with a 10 year time limit)	27
Assumed number of additional second comer transfers <u>between developers</u> on DNO-/IDNO-built metered and unmetered connection projects due to time limit extension	48
Assumed number of additional second comer transfers <u>between developer and DNO</u> (for wider reinforcement) on DNO-/IDNO-built metered and unmetered connection projects due to time limit extension	55

Note;

(1) Figures take from Connections Reporting Pack, average over 2011/12, 2012/13 and 2013/14

(2) Figures from dataset are based on the current regulations.

(3) Figures are rounded.

Source: Ofgem

### Size of Transfer payments

£2014 prices	<b>Second comer to initial connectee</b>	<b>Second comer to DNO</b>
<b>Size of payments</b>	£3,300	£17,700

Note: These numbers represent an average over 2011/12, 2012/13 and 2013/14. Figures are rounded and expressed in 2014 prices.

Source: Ofgem

### Administrative Costs

£2014 prices	<b>To process transfer, check eligibility (relevant for all completed connection invoices with transfers)</b>	<b>To provide quote for notional project (relevant for all quotes with transfers between customers)</b>
<b>Administrative costs</b>	£225	£1,000

Source: Based on stakeholder information. Figures are expressed in 2014 prices.

## **Annex 2 – Updates to the analysis since the primary legislation Regulatory Triage Assessment<sup>10</sup>**

The Regulatory Triage Assessment (RTA) that was prepared as supporting evidence for the Primary Legislation included an early cost benefit analysis of bringing independent connections providers within scope of the Second Comer Regime. No costs or benefits were expected at the primary legislation stage and early estimates were provided for transparency.

This Secondary Legislation Impact Assessment (IA) considers additional amendments. It widens the scope and scale of the Second Comer Regime to include ICP connections but also other amendments, which do not require primary legislation. The additional amendments that have been considered are:

- Bringing connections between distribution systems in scope (not quantified);
- Bringing Section 22 connections in scope (not quantified);
- Extending the time limit from five to ten years (partially quantified); and
- Clarifying the legislation around reimbursing DNOs wider reinforcement costs (not quantified).

### Updated Dataset

Since the RTA was produced, additional data for 2013/14 has become available from the *Connections Reporting Pack*. This IA therefore also considers 2013/14 data. Furthermore, it considers both metered *and* unmetered connection projects.

### Updated Methodology

The RTA used market size and market share information (on exit point basis) from the *Electricity Distribution Annual Report 2010-11*<sup>11</sup>. The ICP market share (on exit point basis) was used to scale the annual average number of second comers on DNO-built connections in the *Connection Data Pack* (on connection project basis) to give the number of second comers on ICP built connections. To avoid inconsistencies, all data used in this secondary legislation impact assessment is consistently sourced from the *Connection Data Pack*.

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<sup>10</sup>[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/388480/Regulatory\\_Triage\\_Assessment\\_Bringing\\_ICPs\\_within\\_scope\\_of\\_ECCR.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/388480/Regulatory_Triage_Assessment_Bringing_ICPs_within_scope_of_ECCR.pdf)

<sup>11</sup> <https://www.ofgem.gov.uk/ofgem-publications/46554/edannualreport201011datapublic.zip>