

DPRC 5 – Initial Consultation

BP Response –Final

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Dear Sirs,

The Power Sector of BEAMA Ltd is the Trade Association representing the principal suppliers of equipment to the UK's Electricity Transmission and Distribution sectors.

Our Members welcome the initiative shown by Ofgem and appreciates the opportunity to express their views.

Our detailed comments are given below.

Nigel Grant
Director

Chapter	Q No	Question	Suggested BPL Response
Chapter 2 - Environmental issues			
2	1	<p>Do you think that evolutionary or revolutionary changes are required to the role of the DNOs to ensure that distribution networks remain fit for purpose?</p> <p>If the latter, in what specific areas does this apply?</p>	<p>Both.</p> <p>In the case of evolutionary, this could be extended by ensuring that any new equipment purchased for use on the Networks is as efficient as possible.</p> <p>One example is Distribution Transformers, where lowest first cost appears to be the main decider in procurement. Ofgem needs to consider how DNO's are incentivised, either by ensuring that greater weight is placed on losses, or by adding to any capitalisation formulae the cost of carbon of the losses.</p> <p>It is notable that the European Commission is actively considering Distribution Transformers in their current consideration of extension to the EuP Directive.</p> <p>Manufacturers can make efficient transformers, it is for the DNO purchasers to order them.</p> <p>Losses could be prescribed, or tax carbon emissions applied - like cars.</p> <p>Additionally in the case of evolutionary, Distribution System Automation is patchy at present and there is a need for more investment.</p> <p>In the case of revolutionary, DNO's need to be incentivised to invest for the long term, ensuring that the networks are made up of equipment that is not operating well beyond normal design life, and is configured of equipment suitable for handling flexibly the anticipated distributed generation capacity.</p>

Chapter	Q No	Question	Suggested BPL Response
			<p>The expected Normal Design Life was just the manufacturer's conservative prediction. We are aware that a number of DNO's are developing a 'health index' for assets based upon several performance criteria with age being one factor to determine when assets need to be replaced. There is no automatic trigger at 20 or 30 years for equipment replacement. We consider this approach to be sensible but suggest manufacturers need to more involved with the DNO's in developing this approach and any associated assessment criteria.</p>

Chapter	Q No	Question	Suggested BPL Response
2	2	Do you think that we have identified the key areas where DNOs can facilitate activities that have a positive impact on the environment?	<p>Whilst you have identified a number, we believe you have not identified how to deal with old inefficient equipment currently in operation on the network.</p> <p>Ofgem should require DNO's to identify either old and/or inefficient equipment and to incentivise DNO's to take this off the network and where appropriate replace this with efficient modern equipment.</p> <p>There is an opportunity in DPCR5 to provide incentives for DNO's to more quickly address the environmental issues surrounding old and / or inefficient equipment in current use on the network. With the exception of low loss transformers replacing old equipment, oil switchgear for example, for modern technology will not in itself have much environmental impact until maintenance costs are considered. The oil needs changing periodically which is a drain on a valuable resource, the refining process contributes to CO₂ emissions as does vehicle exhaust emissions during transportation of the oil to and from site and during disposal. Consideration of these aspects would allow the development of an 'oil asset environmental index' for the installed base. This could be used on an annual basis to indicate the progress made by each DNO and benchmarking across DNO's for this component of environmental impact.</p>
2	3	How do we ensure progress is made on the issues identified with the connection of DG? Should progress be facilitated through a working group or should more formal obligations be developed?	BP has no comment to offer on this topic.
2	4	Do you agree that DNOs should have stronger financial incentives to	Paragraph 2.50 indicates that the losses incentive is working and overall

Chapter	Q No	Question	Suggested BPL Response
		<p>reduce their carbon footprint? Do you think that we have identified the key areas where it may be possible to do this?</p>	<p>network losses have dropped during DPCR3 and DCPR4 to-date. We would suggest that sensitivity analysis is undertaken to determine the potential rate of reduction in losses during DPCR5 under the existing incentive and that of an increased financial incentive. Cost Benefit analysis based upon greater but realistic loss reduction targets could then indicate an appropriate financial incentive.</p> <p>Whilst in principle we agree that there should be stronger financial incentives to reduce the carbon footprint, we believe that in the case of SF₆ used in switchgear the statements in consultation document paragraphs 2.63 to 2.66 do not take into account the full life-cycle and believe that any use of SF₆ containing equipment needs to be set in a wider context.</p> <p>In determining targets for SF₆ gas emission reductions from Distribution Networks consideration should be given to the increasing volume of SF₆ equipment being installed as ageing oil and air insulated switchgear is replaced.</p> <p>In order to develop achievable targets for SF₆ emissions manufacturer's advice should be sought in determining realistic emission levels for existing and known future designs of switchgear that may be introduced during DPCR5.</p> <p>SF₆ gas emissions from Distribution Networks should be considered in the wider context of all greenhouse gas emissions. We urge Ofgem to take account of the content of the Ecofys SF₆ study final report available from http://www.capiel-electric.com.</p>

Chapter	Q No	Question	Suggested BPL Response
2	5	How can the Long Term Development Statements be made more useful for DG and other users of the network?	<p>Our Members believe there is a lost opportunity with the content of the current LTDS's. Ofgem agreed to ambitious DNO capital investment plans by increasing allowances by an average 48%. However, the Ofgem 2007 cost review indicates an average 16% under-spend has occurred for several reasons, one of which is reported as '<i>restricted availability of plant from manufacturers with long production and delivery times</i>'. Our members, who are major providers of equipment or services for the Distribution Networks, would benefit greatly and provide a much improved service to DNO's by having forward visibility of each DNO capital investment plans. We are aware that DNO's submit very detailed information broken down by individual asset type, volume, value and timing in requesting capital expenditure allowances. Accurate knowledge of this would allow manufacturers to better manage and forward plan production, labour and material resources to meet the increased demand. We do not see the need for this information to be confidential as it currently is. The LTDS's could be a vehicle to communicate this information.</p>

Chapter	Q No	Question	Suggested BPL Response
2	6	Is the current regulatory framework constraining a DNO's ability to facilitate low/zero carbon technologies and if so, what could be done to address this?	<p>DNO's could be required to procure the most efficient equipment available at the time of purchase, or equipment of a certain specified efficiency, to ensure that current purchases of capital plant that is likely to be on the system for the next 30 years is not dominated by lowest first cost as is currently the case.</p> <p>The loss reduction incentive should help drive DNO's towards procuring efficient equipment, particularly distribution transformers. However, it should be remembered that the inherent cost of low loss transformers is higher than standard loss design and allowances should be made for this when Ofgem evaluates DNO's submissions.</p>
2	7	We have raised more detailed questions throughout the chapter. We welcome views on these issues.	
Chapter 3 - Customers			
3	1	Do the current regulatory arrangements deliver the levels of service that customers expect?	BP has no comment to offer on this topic
3	2	Is the focus and scope of the current regulatory arrangements correct and are there any gaps that need to be addressed?	There is no monitoring of spend arrangements

Chapter	Q No	Question	Suggested BPL Response
3	3	Are DNOs customer focused enough or should they be doing more to improve communication with customers?	BP has no comment to offer on this topic
3	4	Is DNOs' financial exposure set at the right level and/or do we need to change the emphasis in certain areas?	BP has no comment to offer on this topic
3	5	Do you think we have identified the right issues and appropriate areas for development with the existing incentives?	BP has no comment to offer on this topic
3	6	We have raised some detailed questions throughout this chapter. We welcome views on these issues.	BP has no comment to offer on this topic
Chapter 4 - Networks			

Chapter	Q No	Question	Suggested BPL Response
4	1	Have we captured all the key lessons learnt from DPCR4 regarding cost assessment?	<p data-bbox="1039 336 1919 602">It is unclear to us what measures Ofgem have, or intend to take to ensure the Capital Investment plans of the remainder of DPCR4 and for DPCR5 are robust and delivered. We fully accept that new connection activity is largely outside DNO control and difficult to predict particularly in the current financial climate. However, aged asset replacement should be proceeding in line with the DPCR4 final proposals outlined in 2004. Since information on this is not in the public domain we do not know what areas of the DNO business comprises the under-spend.</p> <p data-bbox="1039 646 1919 878">A further concern is there seems to be no annual capital spend profile either at DNO level or aggregated for all. DNO's are aware of annual project phasing and asset replacement plans and this would be very useful for manufacturers to know in advance in order to plan their procurement and manufacturing activities. Copper and Steel price volatility could be better managed if we had, even an estimated, forward forecast for our equipment.</p> <p data-bbox="1039 922 1919 1393">We would also comment that in reality manufacturers don't experience a 5 year cycle. We note in DPCR4 and previous reviews that the first and last years ramp up and down and the middle three years are effectively the busy times. Manufacturers find this frustrating and difficult to manage. In today's labour market it is difficult to recruit and train the skilled personnel we need to meet the high demand mid cycle only to reduce the workforce in the first and last year. We would suggest Ofgem investigates this trend and encourage and / or incentivise DNO's to better phase projects and asset replacement. A starting point could be to remove the current 5 year averaged spend allowance and adopt a 'use it or lose it' approach on an annual basis linked to a DNO annual forecast capital spend. We recall a capital spend incentive was intended for DPCR4 but this does not seem to be enforced or DNO's do not value the incentive.</p>

Chapter	Q No	Question	Suggested BPL Response
4	2	Is our approach to cost assessment appropriate?	In this chapter Ofgem states that cost information is collected annually. We would suggest given the degree of capital expenditure under-spend and its impact on manufacturers that Ofgem move to a quarterly or half yearly review so there is an earlier opportunity to possibly recover the position.
4	3	Are there alternative approaches to cost assessment that we should be considering?	Refer to our response to 4 - Q1 above.

Chapter	Q No	Question	Suggested BPL Response
4	4	How might our approach to benchmarking be improved?	<p>Refer 4 - Q1 above and in addition benchmarking could be improved by providing greater transparency of DNO capital investment plans, publication of installed asset base age, type and anticipated year of replacement. The 'health' of DNO networks in terms of asset age and technology type could be used to benchmark DNO's against each other. Other areas to consider would be to measure the network available power capacity. This could be helpful to new connection developers in determining locations to site large power projects, wind farms for example.</p> <p>DNO's should also publish by categories of equipment, the % of equipment that is in use on their networks that is in service beyond the normal design life. This should be correlated with their CAPEX performance.</p> <p>Adoption of the above could fall under the category of asset stewardship.</p>

Chapter	Q No	Question	Suggested BPL Response
4	5	Have we captured all the key issues for "networks"?	We believe in asking for responses to the questions raised in this consultation document that Ofgem will have a much greater understanding of all stakeholder concerns.
4	6	Is our building block approach to forecasting appropriate?	BP has no comment to offer on this topic
4	7	What is the scope for developing additional outputs measures and how can these be incorporated into the price control?	Ofgem could consider a new measure of Spend per month against allowance. This would help remove the boom/bust loads imposed on capital equipment suppliers

Chapter	Q No	Question	Suggested BPL Response
4	8	<p>What is the best way for DNOs to gain stakeholder input to their forecast business plans and how should Ofgem facilitate/incentivise this?</p>	<p>BP's Members are critical of both the accuracy of the DNO investment plans and the certainty that any capital expenditure plans will be achieved.</p> <p>The DNO's current under performance is amply shown in figure 4.2. It must be said that it is a surprise that Ofgem does not have more to say about this underperformance and how this will be managed better under DPCR5.</p> <p>Given the lengthy period under which the investment plans are developed, and then verified by Ofgem, it is to be expected that there is a real technical need for these plans. It is therefore a surprise that under-investment can be permitted with seemingly little intervention from Ofgem.</p> <p>Our Members wish to be part of the solution, and there needs to be a stronger understanding that actual delivery of CAPEX extends in a supply chain beyond the DNO's.</p> <p>Stronger planning and organisation for delivery should be a major part of the focus for DPCR5.</p> <p>DNOs should be required to consult with major stakeholders like suppliers to deal with the capacity planning and allied issues.</p>
4	9	<p>Is the IQI and Capex rolling incentive the best way to ensure realistic forecasts and efficient investment?</p>	<p>We consider we have answered this point by the responses above. However, additionally, given the level of under-spend which has consistently increased throughout DPCR4 we do not think the current incentives are driving the behaviour of the DNO's and that Ofgem does not appear to be intervening.</p>

Chapter	Q No	Question	Suggested BPL Response
4	10	How might the IOI and Capex rolling incentive be improved or what additional measures could supplement them?	See response to Q8 above
4	11	Should we aim to equalise incentives on network investment and business costs and how could this be achieved?	BP has no comment to offer on this topic
4	12	Is the timetable realistic?	We feel there are two aspects to this; the DPCR cycle, and product development cycles. As previously mentioned the 5 year DPCR cycle is not being experienced by manufacturers due to ramp up and down in years 1 and 5 respectively. If this could be addressed so manufacturers are not subjected to this volatility then 5 years is appropriate. Any longer and we would be concerned about the accuracy of capital expenditure forecasting, any shorter would not allow sufficient time for consultation. 5 years however is not consistent with new product development of typically 3 to 5 years for capital equipment should new technology be required. If the need can be met by existing equipment then 5 years would be acceptable.

Chapter 5 - Financial issues

Chapter	Q No	Question	Suggested BPL Response
5	1	Should Ofgem use its traditional approach to calculate the cost of capital or should other approaches be considered in order to provide the necessary incentives to invest?	Rate of spend should be the measure
5	2	In particular, should measures to protect DNOs from debt market volatility be considered, such as indexation of the cost of debt, or the use of reopeners at "trigger" levels of interest rates?	Spend should be absolute and in line with the Capex requirements of the network. Any protection should ensure this ability rather than protect the financial performance of the DNO
5	3	Should Ofgem make financeability adjustments or is this a matter for DNOs once the cost of capital is set?	BP has no comment to offer on this topic
5	4	Is it appropriate for Ofgem to be making commitments on investment and its financeability over the longer term?	It is the short term that is problematic. Rates of spend within the period vary widely causing both capacity and personnel training issues
5	5	Should a mechanism for ex-post adjustments for major changes in the tax regime be introduced and, if so, how?	BP has no comment to offer on this topic
5	6	Do respondents support the publication of a fully populated financial model?	Yes

Chapter	Q No	Question	Suggested BPL Response
5	7	Should we calculate the DNOs' allowed revenues in a way that creates a smooth revenue profile over the course of the price control period and seek to reflect the level of costs expected in the last year of the control in order to reduce price changes from one control to another?	Yes
5	8	What factors should we take into account when determining the level of gearing to assume?	BP has no comment to offer on this topic
5	9	Do respondents agree with the proposed treatment of net debt and gearing in ex post adjustments to tax allowances?	BP has no comment to offer on this topic
5	10	What are acceptable alternative approaches to calculating RAV additions; and, following recent market transactions, does RAV continue to reflect the underlying enterprise value of the business?	BP has no comment to offer on this topic
Chapter 6 - Process and timetable			

Chapter	Q No	Question	Suggested BPL Response
6	1	Do you agree with the range of consultation approaches we intend to use throughout DPCR5?	Yes
6	2	Do you believe that we should utilise a consumer orientated challenge group to inform DPCR5?	If a stakeholder approach includes Trade Associations for suppliers
6	3	(? Number not used?)	
6	4	Are there any other ways in which we should look to consult with interested parties?	See 2 above
6	5	Do you agree with our approach to publish specific impact assessments for key "important" decisions?	Yes
6	6	Are there any other key milestones that you believe we should consider for DPCR5?	Spend per year.