

ANNEX

Response to Consultation Paper's Questions

Chapter 2 - Environmental issues

Question 1: 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? If the latter, in what specific areas does this apply?

Whilst the nature, use and demand profiles on networks are changing, the speed of change is slow and is likely to affect different parts of the network at different rates. There is a real risk of unnecessary investment being made if revolutionary changes are made. Hence we believe that evolutionary change is the right way forward.

Question 2: Do you think that we have identified the key areas where DNOs can facilitate activities that have a positive impact on the environment?

We believe that Ofgem has identified the key areas where DNOs can have a positive impact on the environment.

Question 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?

We believe that it is still unclear what, if any, barriers are created by WPD in the connection of DG. We are not aware of any issue raised with us by a generator seeking connection with the process, terms or application of technical standards. Hence, we believe that a working group would be a necessary first step to identify what the evidenced issues are that need addressing.

Question 4: Do you agree that DNOs should have stronger financial incentives to reduce their carbon footprint? Do you think that we have identified the key areas where it may be possible to do this?

We agree that Ofgem have identified the key areas that DNOs can have on their carbon footprint. Whilst a stronger financial incentive may be appropriate, there is little point in doing this without creating measurement systems that accurately measure the effect of DNO actions. Our main concern in this area is the current losses incentive. The settlements system was created as a means to allocate power purchase between suppliers and is also used to allocate network access costs. Whilst the errors in the system are a small percentage of total usage, they are a more significant percentage of calculated losses. This results in a disconnect between the actions that distributors take and the results seen in terms of changes to reported system losses.

Question 5: How can the Long Term Development Statements be made more useful for DG and other users of the network?

Our experience is that most potential connectees (particularly demand connections) prefer to talk to us directly to identify likely connection points to the network. We are aware that an interactive generator connection assessment service has been developed using LTDS information by econnect. The development of this was partly funded by the DTI and we have made the LTDS data available for use without charge. We are not aware of the use being made of this service. We understand that there are concerns from the security service over access to LTDS data over the internet as it is hard to verify users' identity and the reasons for which they need the data. Their preference is for direct communication between DNOs and generators seeking connection information.

Question 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?

Whilst we do not have any evidence that it is a constraint, the current separation of the DG incentive revenue from the rest of allowed revenue results in generator charges being volatile from year to year, as significant scaling of the charges is required to aim towards the incentive revenue. Amalgamation of the DG incentive with the main price control would allow more stability in generator charges.

Question 7: We have raised more detailed questions throughout the chapter. We welcome views on these issues.

Our views on some of the more detailed points raised throughout the chapter are outlined below.

DNO as Facilitator

2.8 The paper highlights the Government's proposals for all new homes to be 'zero carbon' from 2016 and the uncertainty over the extent that zero carbon can be achieved using off-site generation. This decision on on-site or off-site generation is key to knowing how distribution networks will need to develop, as with off-site generation, there is likely to be an increase in the use of electricity for space and water heating, whilst if on-site, a reduction. This has a significant influence on the future design of networks.

It is recognised that there are many ways in which DNOs can reduce their environmental impact, and welcome for example, Ofgem engagement on issues such as fluid-filled cables and management of SF6.

WPD agree that there should be further emphasis on reduction of network losses and a practical starting point is use of lower loss transformers. In pursuing this, it is necessary to avoid distortion of the competitive connections market by having different requirements on IDNOs.

We believe that there is scope to drive worthwhile further reduction in network losses through a more stringent national approach to unmetered supplies.

It is believed that there are gaps in base knowledge on the life cycle impacts of various network design options. WPD have sought to open this arena for debate by

engaging the University of Bath to undertake some life cycle analysis work on a selection of rural 11kV overhead versus underground routes and on early intervention to reduce losses.

Whilst there are a number of initiatives that could be employed to reduce transport fleet emissions, there are some difficulties in achieving a common measurement protocol, as commercial vehicle makers do not currently publish information.

Distributed Generation

2.9–2.19 We agree that DNOs have a role to act as a facilitator in developing a low carbon economy by responding to the changing needs of connectees. The main barrier to actively fulfilling this role is the continuing uncertainty over the volume, voltage level of connection, and location of future generation. As highlighted in Appendix 9, the volume of generation connections forecast to meet the Government's 2010 renewable targets was greatly in excess of those which are actually progressing to connection (noting that the figures in the appendix are for generators that both agreed a connection and have been connected since April 2005 – there are more generators that have been connected since April 2005 but agreed their connection prior to April 2005). Given this uncertainty, the DG incentive has delivered as it flexes with the volume of generation. To date there has been little system reinforcement needed to connect the generation and there is a significant volume (approaching 1GW) of accepted connection offers awaiting the generators instruction to proceed to physical work on the connection.

We agree that whilst there would be benefit in the creation of a national standard connection agreement that gives the template for site-specific information for both DG and all other connections via the DCUSA, we are not aware of concerns with the connection terms that we currently offer.

WPD do not operate a separate connections business. We have always sought to provide a professional and co-operative service to all parties requesting connections. This is partly evidenced by our good record in having no energywatch complaints for over three years, nor determinations, but on a more pro-active note by leading development of connections processes in several areas.

- We favour direct dialogue with those seeking connections, be they Developers, ICPs or IDNOs.
- WPD have long operated arrangements which provide from the outset of an enquiry, a single named Planner and direct contact number.
- Our senior managers meet developers to discuss their needs.
- WPD have lead nationally on developing triangular contract arrangements with street lighting authorities, and have been publicly complimented on this work by those authorities in Ofgem EMSG.

Key to WPD's approach is to treat Customers the way in which we would wish to be treated ourselves; this tenet runs through the Company.

One of the difficulties with the development of technical requirements for DG is that whilst simplified arrangements may be appropriate for very low levels of generator connections, as the level of penetration increases, the need for tighter rules increases to reduce the risk of deterioration in the network performance seen by other network users. These Engineering Recommendations have been developed nationally by all DNOs working through ENA. As they apply at the interface they are also subject to

public comment via Distribution Code Review Panel consultation. WPD are happy to re-engage nationally on this work.

There is increasing concern amongst various Government agencies over the extent of information on critical national infrastructure on public view, and they may comment directly. Cabinet Office has also recently written on the subject of sharing of CNI information with Resilience Forums. It is felt that information such as LTDS statements should not be held on the internet, but be made available on application only.

If it is felt that the content of the LTDS should be amended. WPD are happy to engage in a national discussion, and would seek that any proposed changes are appropriately assessed against effort/benefit.

Whilst a national process for connections has some attractions, we believe that we are currently able to offer a good flexible service and would be concerned at being constrained to a centrally determined lowest common system. The work in ECSG has highlighted WPD's willingness to respond compared to the general service received by connectees.

WPD have received, assessed and made offers approaching 1GW of new distributed generation in Wales, without needing recourse to innovative RPZ measures. Since it appears that the national experience to date is not dissimilar, the drivers to pursue acceleration of RPZ schemes do not seem to currently exist. Providing that Ofgem retain the RPZ mechanism to facilitate them should a greater need arise, then emphasis is probably better focussed on related research activities such as those being undertaken under IFI.

Active network management

2.20–2.24 Whilst further active network management could be encouraged by equalising the incentives for contracting with DG to give support to the system with that for investment in the network, the IIS incentive means that the financial risks associated with non-performance of the generator are significant. The types of penalties in a contract with a generator for non-performance to off-set these IIS incentives are likely to make them unattractive to generators. This, coupled with the relatively low payments that would result from the avoided costs of reinforcement, is likely to make such contracts rare except in very case-specific situations where the costs of reinforcement are prohibitive, such as island connections.

Roles and responsibilities

2.25–2.28 The need for solutions at the interface between transmission and distribution like those considered in the TADG group is dependent on the expected growth in distributed generation. If the draft European targets for the UK for 2020 are to be achieved with a substantial contribution from DG then there may be a need to do something in this area prior to 2015, however on current trends it looks as though the early part of the delivery will be from large scale off-shore wind farms and hence would not necessitate such a significant change to the commercial arrangements in the industry. We understand that the preferred NGT solution is the application of gross charging at the transmission/distribution boundary with DNOs operating as an agent for transmission access. It is unclear to us how this can operate effectively without applying the same principles to customers with generation embedded within their installation – particularly those with an export ability. There is no mechanism to collect the gross data needed for this.

Commercial

2.29–2.33 Many of the generators that connected to the network prior to April 2005 have been connected under a variety of historic charging policies and little reliable data exists prior to 2000. As such it would be almost impossible to re-cost these connections on current connection charge policies and refund the difference between deep and shallowish charges. Given this difficulty and that many of the pre-April 2005 generators did not pay for any deep reinforcement costs as part of their connection charge, it would be pragmatic to include generators into the UoS charging framework after a reasonable period of no UoS charges. 15 or 20 years would appear to be sensible resulting in all pre-1995 connections being charged from 2010 and all generators being charged UoS from 2020.

The framework of the current DG incentive results in any benefits that are attributed to a generator via UoS charges having to be recovered from other generators. It would appear sensible to either recover any benefits that generators give to the network from demand customers or to combine the generation and demand allowed revenues together.

Heat networks

2.25 We believe that addressing the regulatory treatment of and the methodologies used for DG charging will facilitate the development of heat networks.

Energy Efficiency

2.39–2.42 The current industry arrangement is based on a supplier hub principle with the supplier being able to offer a package of energy services including energy efficiency advice. We believe that this is still an appropriate model.

We could also engage with customers to provide information that would help them manage their own electricity use based carbon input. Whilst there are a number of web-sites with elements of information, there is merit in considering, perhaps through ENA, a shared resource along the lines of that on WPD's US parent company web-site, PPL.

www.pplelectric.com/Community+Services/Tools+For+Teachers/Energy+Calculator

The kWh revenue driver was originally included to cater for uncertainty in future load growth. Whilst this uncertainty is still there, the concerns are more about load shifting between parts of the network rather than the overall growth in demand. Hence it would appear sensible to remove this as part of a package including reform of the losses incentive as there is the same concern that this does not provide an incentive to address losses due to the inaccuracies created by the settlements system.

Metering

2.43–2.44 We agree with Ofgem that smart metering should be left with suppliers.

Reactive Power

2.45–2.47 We agree that there should be a cost message associated with poor power factors and that reactive power charging is appropriate. Background general information about power factors, and p.f correction could be included on a DNO web-site, in the same manner as for domestic customer efficiency information mentioned elsewhere.

An area of concern for us is the degradation of performance with age of power factor correction equipment used in street lighting. It appears that there could be significant quantities of street lights operating with poorer power factor than assumed in the calculation of charges to them. We have responded separately to the recent Ofgem

letter on the use of CMS technology which has a measuring capability which may help in this area. It is also an area where further initiatives under the EU Energy Using Products legislation could drive improvement.

Reducing DNOs' carbon footprint

2.48 There is a case for encouraging DNOs to reduce their carbon footprint. WPD has monitored its own CO₂ emissions since 1997, improving the data capture sources along the way. Our approach has been based on (then) DEFRA guidelines. Many of the data streams already exist within businesses for other purposes. We would be happy to give a brief presentation on this and to participate in subsequent Ofgem discussions if desired.

This experience has highlighted a number of issues which impact on the design of any benchmarking or incentive scheme. The ability of a DNO to impact on own emissions will vary:

- Some may have substantially geographically separate licence areas and rely on substantial air travel between them, or to attend national meetings often held in London.
- Some may operate in wide and particularly sparse areas, such as WPD.
- The reporting boundaries may well differ depending on business separation and contracting out e.g. of stores, logistics.
- The age of transport fleets may vary considerably, but as commercial vehicle makers are not required to publish CO₂ figures, very few do. This is different to passenger cars and hence, the benefits of more efficient / lower emission vehicle fleets are difficult to benchmark.
- Generation mix and network losses will have the biggest impact on emissions – these are not within DNO control in the short or medium term.

A key aspect of developing monitoring is that the impact of the distribution businesses is separated from parent companies and other businesses within a group of companies. The DNO carbon footprint needs to be reported separately.

Losses

2.49–2.60 The settlements system was established to allocate unit sales between different suppliers to allow power purchase costs to be settled. The data is also used to establish unit throughputs for TNUoS and DUoS purposes. It is not completely accurate, but as its use is to allocate costs between suppliers, this loss of accuracy affects all parties equally and is not a concern. When however this data is used to try and establish losses, these errors become significant. Increasing the incentive rate using this data will just result in larger windfall losses or gains. As evidenced by the BSC Audit Reports, many of these errors are not corrected later but are written off, hence this is not an issue that cycles out over time but one which can have a permanent bias. These errors do not affect customer bills provided by suppliers as we understand that there is little reconciliation between the data used by suppliers in their billing systems and that in the settlements system.

We believe that there is scope to drive worthwhile further reduction in network losses through a more stringent national approach to unmetered supplies. Ofgem's consultation of 1st April 2008 highlights a number of areas where it is believed that under-estimation occurs and thus increases reported DNO losses. Poor power factor is a further issue with street lighting. The Ofgem consultation specifically comments on:

- Many lamp columns are on longer than desired by the purchasing authority. Consumption is therefore higher than it would otherwise be.
- Energy use of lamp and control gear varies with the age of equipment, meaning the method used to estimate consumption for unmetered supplies can be inaccurate.
- Elexon have investigated the accuracy of estimation for some types of lamp column (of which there are many). On average they found consumption was underestimated by around 10%.
- There is, therefore, little incentive on customers to implement energy saving measures to reduce the level of consumption from public lighting.

WPD believe that there should be further emphasis on reduction of network losses through Alternative 2, and a practical starting point is use of lower loss transformers. In pursuing this, it is necessary to avoid distortion of the competitive connections market by having different requirements on IDNOs. A rapid implementation could be achieved if there could be agreement on some standardised losses for various sizes of distribution transformers. This could benefit supply chain management and avoid competition distortion issues between DNOs and IDNOs. Whilst this may not have the sophistication of an incentive, market-driven approach it does have the merit of simplicity.

DNO own energy consumption, both metered and unmetered, should be captured. WPD have included such GHG emissions within their internal GHG monitoring for several years, based on invoiced quantities.

Given the extent of investment and network disruption that would be required to reduce losses on the existing built network, and the range of other key impacting drivers, there is scope for research on detailed scenario testing. The following issues clearly have a bearing:

- The level and timescale of change of generation mix and effect on kg CO₂/kWhr (figures have varied between 0.41 and 0.54 in a short timescale).
- The impact of Government and personal choice measures on energy efficiency, including zero carbon homes, and effects of energy price rises.
- Impacts of changes in demand through energy-efficient products under EU EUP Directive etc. Moves to hybrid or electric transport.
- Effects of climate change or ratings and customer demand behaviour.

In respect of design of new extensions to the network, WPD believe that there is merit in considering valuation of losses using a shadow pricing related to CO₂ ETS levels, but draw attention to the volatility issues mentioned above. Use of CO₂ valuations would assist in the development of “joined up” Governmental cross sector thinking.

It is believed that there are gaps in base knowledge on the life cycle impacts of various network design options. WPD have sought to open this arena for debate by engaging the University of Bath to undertake some life cycle analysis work on selection of rural 11kV overhead versus underground routes and on early intervention to reduce losses.

Emissions

2.61–2.66 WPD believe that, as a potent GHG, SF₆ losses should be subject to an incentive regime. However, differing compositions of the ages and types of SF₆ equipment on different DNO systems means that care is required in formulating such an incentive. For example, in WPD’s South Wales licence area, the SF₆ holdings

largely comprise high numbers of small volume assets where the kg lost from catastrophic loss of gas from one item is very limited compared to the total holding. In the South West, the situation is significantly different due to the existence of 11 old technology bulk SF6 132kV circuit breakers which represent 30% of the entire holding. Whilst the condition of that equipment does not currently warrant replacement, there is an argument for advancement of replacement on the grounds of environmental risk, and we will include this in our public consultation.

Fluid-filled cables

2.67–2.72 Similarly WPD are pleased that Ofgem have highlighted the issue of fluid-filled cables. Whilst there is some merit in a leakage reduction incentive, the causes and volatility of incidence of leaks make this less workable when, in the case of WPD, there are relatively low quantities of installed fluid-filled cable than in other DNOs. Irrespective of an incentive, we believe that Ofgem support for a replacement protocol based on condition adjusted by environmental risk is necessary in order to retain Environment Agency support for the existing Memorandum of Understanding that currently permits the ongoing operation of these cables on a national basis.

Undergrounding

2.73–2.77 We continue to have concerns over the recovery of the costs associated with network undergrounding in National Parks and Areas of Outstanding Natural Beauty. We are committed to continuing to provide and wherever possible improve on the reliability of our network to reduce both the number and duration of interruptions in electricity that our customers see. An important element of this is investment in the network and undertaking undergrounding of overhead lines for visual reasons would divert resources and investment from this essential activity. We will seek views on our position as part of our public consultation.

Chapter 3 – Customers

Question 1: Do the current regulatory arrangements deliver the levels of service that customers expect?

We believe that current regulatory arrangements generally work well and in the main deliver the levels of service that customers expect. There are some areas where we believe the current arrangements could be improved.

The Interruption Incentive Scheme

The IIS has worked well in reducing both the number and duration of interruptions to supply and WPD believe that these measures continue to be of prime importance to customers. We would support the continuation of the IIS incentive scheme for DPCR5. The target setting methodology used in DPCR4 should be continued.

Telephony Incentive Scheme

We believe the current Ofgem telephony survey has limited value in providing clear messages to improve performance and could benefit from being simplified. The survey provides a purely subjective measure of performance and we strongly believe the incentive should be strengthened to cover objective measures such as the speed of response and the number of unsuccessful calls to a DNO contact centre.

Guaranteed Standards of Performance

The second stage of the WTP survey should establish more clearly the exact relationship between the costs to put proposed new or tightened standards in place and the willingness of customers to pay for these improvements. It is important that any subsequent changes to the standards of service accurately reflect these findings.

Customer Service Reward Scheme

The customer service reward scheme has been successful in encouraging DNOs to improve service in areas that cannot be easily measured or incentivised through more mechanistic regimes. We support its continuation into DPCR5 but do not feel it is an appropriate mechanism to incentivise a DNO's performance in tackling climate change. We believe this requires a stronger incentive based on a clear set of measurement principles and outputs.

Question 2: Is the focus and scope of the current regulatory arrangements correct and are there any gaps that need to be addressed?

We support the work that Ofgem is proposing on worst-served customers. We believe the most appropriate mechanism to do this is one that focuses on improving the overall average reliability of worst-served customers where targets are set and appropriate incentive levels are determined to reward good performance and penalise poor performance.

We do not support the introduction of a Guaranteed Standard Scheme which provides compensation for worst-served customers but does not address the underlying cause of the problem or provide anything more than a weak incentive to encourage DNOs to improve the reliability of the supply.

An incentive for worst-served customers would benefit only a small minority (<0.5%) of total customers. The incentive should not be an alternative to continued improvements in average performance for all customers.

Question 3: Are DNOs customer focused enough or should they be doing more to improve communication with customers?

We have commented in response to Question 1 on the need to include objective measures in the telephony incentive in addition to the customer satisfaction attributes.

We would welcome investigations into the potential widening of the incentive scheme into DNO customer focus and customer communication

Question 4: Is DNOs' financial exposure set at the right level and/or do we need to change the emphasis in certain areas?

We believe that a DNO's financial exposure is generally set at the right levels.

We would not support the financial exposure under the IIS scheme being increased from the current $\pm 3\%$

We would like to see the unlimited financial exposure under the Guaranteed Standards reviewed in the event of a high impact low probability event.

Question 5: Do you think we have identified the right issues and appropriate areas for development with the existing incentives?

We believe that Ofgem have broadly identified the right areas for development.

We note that there has been an increase in short interruptions during to DPCR4. We believe that this is a consequence of the focus on reducing longer interruptions by the increased development of automation schemes. WPD believe that customers prefer frequent, short power cuts over long, infrequent power cuts and we do not support any changes to the existing treatment of short interruptions.

Question 6: We have raised some detailed questions throughout this chapter. We welcome views on these issues.

Our views on some of the more detailed points raised throughout the chapter are outlined below:

Introduction

3.2. We agree that the existing quality of service incentives are working well and have delivered measurable benefits for customers. We would support the continuation of the IIS incentive scheme for DPCR5.

We support investigations into the potential widening of the incentive scheme in the areas indicated namely:

- Worst-served customers.

- DNO customer focus and customer communication.

We would be happy to work with Ofgem to develop an incentive for worst-served customers and to ensure that customer communication and complaint handling incentives are strengthened in response to the changes that will result from the implementation of the CEAR act.

3.3 The IIS incentive scheme is successful because it focuses on the prime measures that matter to customers i.e. the frequency and duration of interruptions as well as the quality of the telephone response they receive.

It is WPD's view that improvements in these three key areas will continue to be important to our customers.

Who are DNOs' customers?

3.4 We agree that there is a range of end-users for the network and that these are as outlined. The mix of these customers will vary significantly between Companies and an important part of the stakeholder engagement and business planning process will be to incorporate potentially diverse views into a single cohesive plan that fairly represents all customers. WPD's customer base (2,500,000 approximately) is over 90% domestic customers and we operate a predominately rural network.

There is an important distinction between minority groups of customers who require additional protection and minority lobby groups who, although vocal, are not representing the views of the majority of customers.

3.5 We support additional arrangements for vulnerable customers and customers who are worst-served providing that the additional cost of providing the enhanced service level is recognised within the overall price control settlement. It is unlikely that these kind of initiatives can be justified on a "willingness to pay" basis given that improvements for worst-served customers will, in WPD's case, effectively require customers in urban areas to agree to fund improvements for rural ones.

What do customers want?

3.6 We support the work that Ofgem have carried out on customer research as part of DPCR5 so far. The work has, in our view, been specified to a sensible level of detail and executed well thus far. We do not however, think it is appropriate to draw any conclusions at this stage as the preliminary findings outlined in the document are based on an initial pilot study only. The next stage of the project which will test customers' willingness to pay across different geographic/demographic areas will be an important milestone in setting out customers' expectations clearly.

3.7 WPD have previously carried out customer research using the facilities of a market research agency to inform the business strategy and planning process. We do not intend to replicate the work that Ofgem is undertaking for DPCR5 as part of its willingness to pay work, although we expect to undertake research in specific areas to inform the business planning process. We will be happy to share the outcome of this research with Ofgem.

In addition to external research outlined above, we carry out a weekly in-house survey from our contact centre, predominantly to establish the views of customers who call us to report a "no supply" call. Our contact centre survey can be tailored to get customer's views on specific areas e.g. customer views on messaging systems or on

the service they receive when requesting a connection. Again we will be happy to share the results of this survey work with Ofgem as part of the DPCR5 process.

Apparent resistance to paying for quality of supply improvements

3.8 As stated in 3.6, we do not think it is appropriate, at this stage, to draw any conclusions from the qualitative phase of the Customer First research. We agree the views obtained thus far may not be representative of all customers' views.

3.10 We agree that arrangements for worst-served customers merit particular attention and look forward to working with Ofgem to define a "worst-served" customer.

Importance of good communication during power cuts

3.11 We believe that customers continue to place a high priority on receiving accurate and up-to-date information during a power outage and this is supported by our own weekly in-house survey. We believe the current Ofgem telephony survey has limited application and could benefit both from being simplified but also by being extended to cover objective measures such as the speed of response and the number of unsuccessful calls to a DNO contact centre. Total unsuccessful calls comprise:

- Total calls not reaching the specified lines.
- Total calls terminated by the DNO during the IVR/group announcement.
- Total calls not allowed in the queue or flushed from the queue.
- Total calls abandoned by the customers in the queue.

This information is already collected by Ofgem and could be audited as part of the annual IIS audit to ensure that the data is being reported in a consistent way between Companies.

Importance of environmental issues to customers

3.13 WPD support the continued research into customer's willingness to pay for environment measures and specific issues such as replacing overhead lines with underground cables, particularly in National Parks. It is important that the conclusions of any research in this area reflect the views of the majority of the DNOs customers who will be required to fund any initiatives. We will seek views in this specific area as part of our business plan public consultation.

Connections services are still an issue for some customers

3.15 We agree that customer complaints to Ofgem and to *energywatch* provide a useful indication of areas of concern for customers. WPD is particularly proud of its customer service record which includes zero *energywatch* complaints for 38 months (at March 2008) for both WPD South West and South Wales. WPD are the only DNO to achieve a "zero *energywatch* complaint year" and *energywatch* statistics show that there are wide variations in performance between companies.

Table 3.1 indicates that since April 2006 there have been 11 Authority formal connection determinations and 140 occasions when informal advice has been offered, almost entirely related to connections. WPD work hard to ensure that we treat customers as individuals and resolve any issues with them directly. We have not had any determinations during this period nor are we aware of any cases having been referred to Ofgem for informal advice. Ofgem should incentivise Companies to deal with customers as part of their complaint handling process and not to seek determination from Ofgem.

3.16 WPD has been heavily involved in the setting up of the Energy Ombudsman Scheme to meet the requirements of the CEAR Act. We believe that we have demonstrated by our actions that we are an extremely customer-focussed DNO.

3.17 WPD's internal complaint figures for 2007/08 based on a total of 462 complaints can be broken down as follows:

Quality of Supply	40%
Equipment Query	22%
Site Works	19%
Connection Related	8%
Other	11%

This breakdown is consistent with previous years. We expect that these numbers will rise following the introduction of the Complaint Handling Standards in July 2008. The Complaint Handling Standards will increase the number of complaints that are logged due to changes in the definition of a complaint and a requirement to log complaints that are resolved at the first point of contact.

Current arrangements and development for DPCR5

Our comments on table 3.18 are covered in our separate response to Appendix 7.

Consumer redress

3.20 WPD has been heavily involved in the setting up of the Energy Ombudsman Scheme to meet the requirements of the CEAR Act. We have been voluntary members of the Energy Ombudsman Scheme since April 1 2008 and have been working with Ofgem and the service provider to understand the requirements for a statutory scheme.

The set up costs of the scheme (incurred 2006/07) together with the ongoing running costs of an Ombudsman scheme will be included within our overall business plan.

Complaint handling

3.21 WPD believe that the new redress scheme and complaint handling standards will adequately address the DNOs' complaint handling process. We do not consider that a further Guaranteed Standard is necessary.

Consumer representation

3.23 The use of a small consumer-oriented challenge group may be appropriate providing that;

- A wide range of views and expertise is represented.
- Single issue groups/views do not dominate.
- The panel is able to meet regularly and is well briefed on distribution issues, especially if they are to advise the Authority sub-committee on "the more complex and technical issues" associated with DPCR5.

Quality of service interruptions incentive scheme (IIS)

3.24 We agree that the IIS has worked well in reducing both the number and duration of interruptions to supply. WPD believe that these measures continue to be of prime importance to customers.

The Quality of Supply Working Group worked with Ofgem during DPCR4 to identify an effective method of comparing quality of supply and consistent target setting. WPD welcome Ofgem's statement that this methodology should continue to underpin target setting for DPCR5.

As a frontier DNO for CML performance we would support an option to be given an allowance to support a target that reflects our current level of performance. This would lock in the current level of performance for DPCR5 and encourage further improvement for customers' over the price review period.

Frontier performance is a valuable mechanism for revealing what DNOs are able to achieve. Where there are wide differences in performance, that cannot be explained by network differences, such as those that exist with average restoration times, then a principle was established in DPCR4 that the frontier performing DNOs were recognised and rewarded. It is our view that this frontier performance in relation to average restoration time should continue to be rewarded in the same way as in DPCR5.

3.25 WPD supports the development of an incentive to improve service to worst-served customers. Our preference will be for a scheme that incentivises DNOs to improve the overall average reliability of worst-served customers either by operational means or by network investment. WPD believe that this is a more appropriate mechanism than a compensation scheme which does nothing to remove the underlying cause of the poor performance.

3.26 The increase in short interruptions is a consequence of reducing long interruptions, particularly where automation schemes have been introduced. We believe that customers are tolerant to short interruptions of less than three minutes duration when the alternative would be being off supply for a much longer period of time.

3.27 We do not support the option of equalising CI incentive rates across all DNOs. The current approach, of different CI incentive rates across DNOs, generally enables the better performing DNOs to secure greater rewards for outperforming their targets. This is appropriate as it is more difficult for the better performing DNOs to outperform their targets. In addition in order to equalise CI incentive rates it would be necessary to vary either or both of the percentage revenue exposed to IIS and the bandwidths around the IIS targets across DNOs. This would expose inequitably the DNOs to differing degrees of risk.

3.28 Network performance in any one year can be influenced by either:

- An exceptional event (e.g. severe weather on one or two days); or
- A one-off exceptional event – a single major event which has a material impact on a DNOs annual performance.

The DPCR4 process-defined thresholds for these types of event and exceptional events in either of the above categories were excluded from both the target setting process and the valuation of whether a DNO has delivered against their targets.

The associated Ofgem audit process ensures that DNOs carry out appropriate mitigating actions and that DNOs are incentivised to perform well during exceptional events. There are a number of other standards, such as the Guaranteed Standard for supply restoration in severe weather that also maintain an incentive on a DNO to

perform well during an event that may potentially be excluded from its annual performance.

Ofgem could further ensure that there is a further incentive on DNOs to perform well during exceptional events by incorporating into the audit process a measure of how quickly a DNO restored its customers, either by comparing restoration across companies affected by the same event, or by benchmarking restoration performance with similar events that have been historically excluded from the IIS scheme. A company could expect to have all of its CML excluded only if it met the benchmark criteria.

WPD believe that the exclusions mechanism has worked well and made consistent comparisons of underlying performance between DNOs achievable. We cannot see merit in changing the thresholds, given the work required on resetting of targets and the difficulty that changing the criteria will introduce in making long run comparisons of data over price control periods. It would be a complicated process with no benefit to either company or customer.

Quality of telephone response

3.29 We believe that the customer survey on quality of telephone response is of limited value in understanding how well a DNO communicates with its customers and provides only a small incentive on DNOs to improve communication with its customers.

3.30 Whilst WPD have been pleased to be the recipient of a small reward in this area, there appears to be an inherent bias in the consumer survey. All safety and security telephone calls for WPD South West and WPD South Wales are handled at one central contact centre. There is no distinction between the way in which these calls are routed or handled. Operators deal with all calls for either company, as they arrive, using one process. Despite this, we have noticed big variations in the monthly results and also, on occasions, the rolling twelve month figures. For example, in April 2007, WPD South West was in eighth position in the league table rising to first position one month later. Over the same period WPD Wales fell from 2nd to 4th. We are struggling to understand these results and believe that it will be difficult to widen an incentive scheme that is based on subjective data which provides a DNO with no clear messages for improvement.

Any broadening of the survey to cover other areas, should therefore in our view be supported by objective measures.

3.32 In WPD we have a sophisticated messaging system, which plays a customer a tailored, specific message and allows them to automatically register when they call in to report a no supply. Our own customer survey indicates a high level of satisfaction and acceptance of the message, with typically 70% of all customers contacting us using the automated system.

This potentially means that the survey sample provided to Accent, which is based on customers who speak to an operator only, is a small subset of all customers contacting WPD. It is possible that this subset of customers represents a biased sample that may be less satisfied than the majority who has received the message and chosen not to speak to an operator.

We agree with the proposal that customers who receive an automated telephone response should be included in the survey to provide a balanced view from all customers. We do not believe that there any data protection legislation issues and we

would be happy to provide this data to Accent on the same basis as the data currently provided on customers who talk to an agent.

Guaranteed standards of performance

3.34 The second stage of the WTP survey should establish more clearly the exact relationship between the costs to put proposed new or tightened standards in place and the willingness of customers to pay for these improvements. It is important that any subsequent changes to the standards of service accurately reflect these findings.

3.36 With regard to compensation payments to business customers, the guaranteed standards were intended to compensate customers by exception where an expected level of service was not met as opposed to compensate for consequential loss. The appropriate protection for business customers, in WPD's view, is to take out insurance.

Customer service reward scheme

3.47 We support the Ofgem discretionary reward scheme and the areas of current focus. We would support its continuation within a package of incentives throughout DPCR5. We believe the current scheme could be further improved by:

- Earlier indication of the areas of focus to give DNOs a longer lead time to develop and implement appropriate initiatives.
- Fewer areas of overlap between the different areas of focus and a less prescriptive approach to the criteria required in each category.

3.48 The discretionary reward scheme, by definition, encourages DNOs to improve customer service that cannot be incentivised through more mechanistic regimes. There is no direct correlation between investment and reward and in this respect the incentive is only weak. Its true value is in the recognition that a successful DNO receives for carrying out initiatives to deliver service over and above its minimum licence conditions.

3.50 For reasons outlined above, it is difficult to understand how this type of incentive is appropriate for DNOs to tackle climate change. We believe this requires a stronger incentive based on a clear set of measurement principles and outputs.

3.51 We do not support incorporating best practice initiatives from DPCR4 into the licence conditions of all the DNOs for DPCR5.

Chapter 4 – Networks

Question 1: Have we captured all the key lessons learnt from DPCR4 regarding cost assessment?

The main weaknesses of DPCR4 regarding cost assessment were:

1. The poor quality of the data
 - Cost categories were undefined.
 - Cost categories included absorbed overheads so devaluing cost comparison.
 - Cost understanding poor; for example, related party accounting.
2. The over-reliance on statistical techniques
 - The quality of data must be robust before embarking on cost comparisons.
 - Statistical techniques are secondary to an understanding of the cost function.

The IQI mechanism adopted in DPCR4 has been partly a success:

- It is right that DNOs who forecast capital expenditure close to the Ofgem assessment should be rewarded with additional income.
- However, in the absence of any measurement of output and efficiency measures, it is inappropriate to reward DNOs whose actual spend is less than their capital expenditure allowance. In reality such under-spend is more likely due to capital deferment than to real efficiency.
- Likewise it is inappropriate to penalise DNOs whose actual spend is more than their capital expenditure allowance, provided such DNOs can demonstrate that the investments they have made are necessary to meet licence and statutory obligations/responsibilities and have been spent efficiently.

Question 2: Is our approach to cost assessment appropriate?

Cost comparison requires both a methodology that works and the right data to which the methodology can be applied. We agree in broad terms with your approach.

However, we make the following comments with regards to Ofgem's intentions to:

- improve investment incentives
 - the IQI mechanism should be removed with respect to actual capital expenditure
- remove incentives to categorise costs in a certain way in order to maximise RAV additions
 - The use of related parties may contaminate the data used to compare costs by reclassifying indirect costs as direct costs. We have already made detailed submissions to Ofgem in relation to this and would draw your attention to them.

Ofgem's development of the RRP has eliminated the need for an "HB PQ" but:

- a. The work to identify and document the cost drivers for each activity should be pursued with great urgency as its conclusions will need to be used in conjunction with consistently prepared cost data for a robust result to the price review.
- b. Much work is still necessary to ensure consistency of data; Ofgem in their autumn visits should focus their attention on apparent out-of-line reported activity costs ("outliers").
- c. Identifying cost drivers should proceed as a matter of urgency, but will not yield useful results until consistent data is available.

Question 3: Are there alternative approaches to cost assessment that we should be considering?

The key issue with cost assessment is the quality of the data, and how the data should be assessed in light of the cost drivers for each activity. Once these are available alternative approaches would provide, at best, a "cross-check" of the result.

Question 4: How might our approach to benchmarking be improved?

A lot of progress has been in ensuring data comparability through the development of the RRP. However, more work has to be done as noted in our responses to questions 1 to 3 above.

The next step is to properly understand the cost function for each activity. For the cost data range of DNOs, costs increase in a linear fashion from a fixed point. The cost function is therefore as follows:

$$y = ax + b$$

- where "y" is the cost, "x" is the cost driver, "a" is the variable cost slope and "b" the level of fixed cost

In relation to each element of the general formula:

1. "x". Progress has been made between the DNOs and Ofgem establishing that underlying cost of direct activities is driven by the asset base.

With respect to indirect activities it is recognised that network scale is a key underlying driver:

- CSV: is only a proxy for scale so is not that relevant to the costs it is driving.
- MEAV: although more relevant, is a measure of asset value; assets do not necessarily create work in proportion to their value.
- Man Hours: we support the initiative by Ofgem to attempt to determine network scale by the development of an asset man-hours driver. This scale variable will determine the time taken to complete a particular operation and the number of times the operation is required in a year. We will reserve our judgement on its applicability until it has been developed.

We agree that some indirect activities notably IT and Telecoms and also Property Management should be examined separately.

2. “b”. A critical input into benchmarking is the determination of fixed costs for an activity:
 - The definition of fixed costs is those costs that do not vary with a change in units/output over the range of data points under consideration. For example, procurement is a fixed cost; if network scale increases, the value of contracts increases, but the number of contracts stays the same.
 - Fixed cost should be set in the context of the 14 DNOs operating in the UK. The 14 DNOs operate within a requirement for core competency. For example, all DNOs require a network policy team proficient in electrical engineering.
 - The determination of fixed costs should be determined by adopting a bottom-up approach by activity.
3. “a” The slope of the line will be determined from the variable “x” and “y” and the fixing “b”. It is important that there is a proper understanding of the slope of the line:
 - A steep slope might suggest that fixed costs are too low.
 - A flat slope might suggest that fixed costs are too high.

Question 5: Have we captured all the key issues for “networks”?

Dealt with in answers to other questions.

Question 6: Is our building block approach to forecasting appropriate?

Yes

Question 7: What is the scope for developing additional outputs measures and how can these be incorporated into the price control?

It may be possible to develop an output measure based on Health Indices to give a measure of the overall system health. At present these systems are still developing and hence, basing a regulatory reporting requirement or incentive on them risks ‘fossilising’ them in an under-developed form. If such an output measure is to be used, then it will need clear rules and an audit regime to ensure comparability between companies. If an associated incentive were to be planned then it would need to start at a low level whilst systems were robustly established.

Question 8: What is the best way for DNOs to gain stakeholder input to their forecast business plans and how should Ofgem facilitate/incentivise this?

We welcome the opportunity to involve customers and other local stakeholders in developing our overall investment plans. The customer research already undertaken by Ofgem has been helpful in identifying the main issues that we should include in our consultation.

We aim to engage a wide range of stakeholder from across our region to ensure that our Business Plan benefits customers as a whole, rather than individual stakeholder interests.

On 30 May we will be launching a stakeholder consultation via our website. We are also proactively mailing out to a wide range of regional stakeholders. We are planning regional stakeholder events later this summer. We will also be talking to specific stakeholder organisations such Regional CBIs to highlight the consultation.

Ofgem has made it clear that stakeholder engagement is a requirement; therefore we do not believe that an incentive is necessary.

Question 9: Is the IQI and capex rolling incentive the best way to ensure realistic forecasts and efficient investment?

The IQI mechanism is appropriate in rewarding those DNOs who forecast capital expenditure close to the Ofgem assessment.

However, in the absence of any measurement of output and efficiency measures, it is inappropriate to reward DNOs, through the capex rolling incentive, whose actual spend is less than their capital expenditure allowance. In reality such under-spend is more likely due to capital deferment than to real efficiency.

Likewise it is inappropriate to penalise DNOs whose actual spend is more than their capital expenditure allowance, provided such DNOs can demonstrate that the investments they have made are necessary to meet licence and statutory obligations/responsibilities and have been spent efficiently.

Question 10: How might the IQI and capex rolling incentive be improved or what additional measures could supplement them?

It is difficult to determine whether under-spent capex is due to deferment rather than efficiency, and whether overspend is due to need rather than inefficiency. Therefore, the rolling capex incentive is inappropriate. Rather, the RAV should be adjusted for actual capex at the end of the review period, subject to Ofgem determining whether the capex has been efficiently spent.

Question 11: Should we aim to equalise incentives on network investment and business costs and how could this be achieved?

The approach proposed above in Q10 would mean that the incentive to make savings on RAV additions and opex business costs would be equalised:

- An efficiency saving made on RAV additions would be retained in the RAV over the life of the asset plus a rate of return to compensate for the time loss of value.
- The benefit from an equivalent saving made on business costs, which are not added to the RAV, would be fully realised in the same year as the saving.

Question 12: Is the timetable realistic?

We welcome Ofgem clearly laying out a timetable with specific dates for business plan submissions. The timetable is realistic.

Chapter 5 - Financial issues

Question 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?

Ofgem should continue with the traditional approach to help ensure a consistent and predictable regulatory environment. A more predictable regulatory environment provides investors with more certainty and in the past has benefited customers by ensuring a low cost of capital.

Question 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 re-openers at “trigger” levels of interest rates?

DNOs have good access to capital markets and bank funding and as such have been encouraged by Ofgem to regard cost of capital part of incentive regulation. Therefore, provided that the cost of capital has not been set aggressively, there is no need for further protection against financial market volatility (in the same way that there is no protection within capex for commodity market volatility).

There is no need for interest rate triggers because companies are able to manage their funding risk using freely available financial market products.

Question 3: Should Ofgem make financeability adjustments or is this a matter for DNOs once the cost of capital is set?

Ofgem should set an appropriate cost of capital so as to ensure that financeability adjustments for individual companies are not required.

Question 4: Is it appropriate for Ofgem to be making commitments on investment and its financeability over the longer term?

The agreed investment programmes for DNOs having been entered on the Ofgem financial model will output key financial ratios. Ofgem should set an all-DNO cost of capital which ensures that the credit rating agency financial ratio tests should be met by a well-managed DNO

Question 5: Should a mechanism for ex-post adjustments for major changes in the tax regime be introduced and, if so, how?

Given the significant impact that tax adjustments that are outside the control of a DNO can have, it would be prudent to set an “acceptable band” around the tax allowance. If ex-post changes in the tax regime would have resulted in a change in the tax allowance for a DNO that was more or less than an acceptable band, then a tax adjustment would be made. An acceptable band could be 1% of the allowed revenues over the period of the price control.

Question 6: Do respondents support the publication of a fully populated financial model?

Yes we fully support the publication of a fully populated financial model.

We support the publication of a fully populated financial model. The RRP has provided openness and clarity enabling significant errors and inconsistencies to be spotted by other DNOs, resulting in changes required by Ofgem. The same principle can be extended to the publication of a fully populated financial model.

Question 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?

A smooth profile is preferable

Question 8: What factors should we take into account when determining the level of gearing to assume?

The level of gearing assumed should be consistent with Ofgem's target Credit Ratings, both in terms of Debt to RAV ratio and interest and cash flow coverage ratios.

Question 9: Do respondents agree with the proposed treatment of net debt and gearing in ex post adjustments to tax allowances?

Yes

Question 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?

The enterprise value of a company or a DNO is commonly determined by future cash flows discounted at an appropriate rate. For a DNO the enterprise value is calculated by reference to RAV because the RAV is the economic value of the underlying assets.

Chapter 6 - Process and timetable

Question 1: Do you agree with the range of consultation approaches we intend to use throughout DPCR5?

We welcome the early setting out of the DPCR5 process, consultation approach and timetable. It will enable companies to plan their DPCR workload and identify potentially busy periods. In this respect it will be important that the timetable is adhered to by both DNOs and Ofgem as the failure of any one party to meet a deadline will inevitably impact on others.

The timing and content of the December 2008 policy paper will be very important to the companies who are required to submit detailed business plans in January 2009. We welcome Ofgem's intention to close off key policy issues as early as possible to reduce the degree of uncertainty on DNOs and provide a firm basis on which to submit their plans for 2010-2015.

There will need to be some time allowed for the companies to absorb the implications of the proposed policy paper before submitting these business plans. Clearly the earlier in December that the policy paper is published the better the companies' ability to understand and incorporate its contents into its business planning process will be.

There are a number of areas where Ofgem are indicating a different approach from previously, notably the reduced number of formal written consultation documents and the increased focus on stakeholder engagement. Whilst we are open to Ofgem taking a different approach to how it communicates its thinking in the latter stages of the price control review, we believe that the September update paper at previous reviews played a useful part in the process. We encourage Ofgem to consider some form of quantified statement on the key positions around September 2009

Question 2: Do you believe that we should utilise a consumer orientated challenge group to inform DPCR5?

There may be benefit in utilising a consumer-oriented challenge group to inform DPCR5. The value of group will be dependant on a range of factors, in particular that:

- A wide range of views and expertise is represented.
- Single issue groups/views do not dominate.
- The panel is able to meet regularly and is briefed by Ofgem on distribution issues, especially if they are to advise the Authority sub-committee on "the more complex and technical issues" associated with DPCR5.

Question 4: Are there any other ways in which we should look to consult with interested parties?

The document proposes a wide range of consultation by both Ofgem and the DNOs by a variety of different methods. In particular, the theme of stakeholder engagement is a significant new feature of the price control process.

It would be useful for Ofgem to review the experience of DNO stakeholder engagement as part of the "Lessons Learned" exercise at the end of DPCR5.

Question 5: Do you agree with our approach to publish specific impact assessments for key "important" decisions?

We agree with Ofgem's approach to publish specific impact assessments for key "important" decisions.

Question 6: Are there any other key milestones that you believe we should consider for DPCR5?

We cannot identify any other key milestones other than those identified within the document.