

Ofgem RIIO2 Process - WWU Concerns 1 September 2020

During the WWU and Ofgem bilateral meetings on 11 and 24 August we raised a number of concerns about the RIIO2 draft determination process. This document is a formal record of our concerns which significantly undermine the quality and robustness of the price control process.

1. Inconsistencies between GDNs

Repex - Ofgem's approach to disallowances in mains replacement is inconsistent between networks, is not reflective of the requirements of the safety case and is creating a postcode lottery across the UK. It is important this is reviewed and that the consequences are fully understood, and decisions on workloads are consistently applied.

CVP - Ofgem have not compared or checked the rewarded CVP commitments against the existing performance of other companies. NGN were given a CVP reward based on their commitment to improve responses to repairs by the end of GD2; the level of their commitment is broadly aligned to what we've already achieved in 2019; yet no reward has been given to WWU for our BAU performance which is already exemplar. This is neither fair nor representative of consistent treatment. We would urge Ofgem to look at this ahead of the FDs.

Cyber OT - further to our letter dated 19 Aug 2020, we note that some networks have received a base allowance for their Cyber OT expenditure. However, we have been told that our expenditure will have to be dealt with through a reopener because your team have insufficient time to assess our investment which we offered to submit in full on 4 September; over 3 months before you issue your FDs. The regulatory regime needs to offer networks a level playing field and we look forward to working with you to support the base allowance of 0.05% of RAV as a minimum for WWU ahead of the reopener window.

IT – we were disappointed at the lack of engagement between BP submission and DDs in respect of our IT Capex investment, with very few supplementary questions, no requests for bilateral meetings and yet our allowances were cut by 80% unlike some of the other GDNs.

2. Policy changes introduced without prior consultation

Cost assessment - we are disappointed there was no discussion in advance of the DDs about the move to the 85th centile as a benchmark. The justification given for this is that this is supposed to set the benchmark at the second most efficient network, however, there are errors in the modelling to achieve this, which calls this into question. We request Ofgem revisit this ahead of FDs.

Cost assessment - the use of a single model was not consulted upon prior to the DDs and the reliance on just one single Totex model is not robust. This is demonstrated by the deterioration in the R^2 between price controls from 0.93 to 0.87. This approach has also been discouraged by the CMA in other regulated industries. We urge Ofgem to review the cost assessment toolkit in line with proposals included in our business plan and DD response.

NARMS - we are concerned that despite extensive engagement on NARMS there was a last minute change of policy which changes the sharing mechanism to 95/5 sharing mechanism compared to the c. 50/50 for all other expenditure. This only appears in the detailed NARMS annex and is not being consulted upon in the mains DD documents. It is also not clear that Ofgem have considered this sharing mechanism in their holistic assessment of the package offered to GDNs. This is a significant policy change which adversely affects our ability to innovate and respond to changes required by stakeholders which needs to be reconsidered ahead of the FDs.

CSAT - we welcome the engagement to date through the Customer Working Group however we were not consulted on Ofgem's DD proposal for an asymmetric dead-band - this will disincentivise companies to invest in continuing to drive up customer satisfaction scores. We ask Ofgem to reconsider this asymmetrical approach.

3. Errors & lack of assurance

Modelling errors - we have been disappointed by the number of errors we have found in the cost assessment modelling, for example the use of incorrect MEAV numbers and copy/paste errors. This questions the level of assurance Ofgem undertook prior to issuing the DDs. This assurance must be more robust going forward and we ask that networks have the opportunity to review models in advance to avoid similar embarrassment for Ofgem in the FDs.

Incorrect allowances due to errors - the inaccuracies we have found have the potential to change allowances and the benchmark significantly. We are concerned that Ofgem are not proposing to correct and reissue their own models or the outcomes; instead they are asking companies to make these amends themselves to the Ofgem models which is wholly inappropriate. Stakeholders will be responding to the DDs based on inaccurate modelling and incorrect allowances; this does not provide a robust consultation process and this needs to be addressed.

DDQ process - we welcome the introduction of the DDQ process given the number of queries we had on the DDs, however the process was slow; with 21 questions taking at least 8 working days to receive a response which has greatly limited the time available to analyse and respond to the consultation. Disappointingly the quality and depth of many of the responses has been poor, for example 14 of the responses said this would be dealt with at a meeting which was held on 24 August. Whilst topics were discussed, the majority of questions were not fully answered. It has also been held too late to give time to consider in detail before DD responses.

4. Bilateral meetings and working groups

Cost assessment - after good engagement leading up to DDs we were concerned firstly at the late offer of a working session to demonstrate the complex workings of the cost models; four weeks in to the 8-week consultation process. Additionally, the CAWG meeting wasn't scheduled until 14 August; which given the volume of errors and queries, was too late in the process. So much so, as mentioned above, the networks are now being asked to correct models for errors because there is no time left for Ofgem to do this which is inappropriate.

NARMs - we have worked effectively with Ofgem in developing NOMs for GD1 and latterly NARMs for GD2. Our concerns on the principles of NARMs will be contained in our DD response however from a process perspective we are concerned at the significant data request received mid-August; such a late stage in the process. We request that senior officials in Ofgem become more involved in the decision making on NARMs ahead of the FDs to ensure its appropriate, proportional and delivers value.

Other bilateral meetings - conversely, we would like to thank the Ofgem teams for the positive engagement via our bilateral meetings on IT, Engineering and with the wider team; we would welcome more of this constructive debate.

5. Timelines and FD process

Late issue of working files and models - a number of the working files and models were issued late with some files (e.g. Stata file) only being made available on 7 August. We have only been provided with the detailed middle-up and bottom-up models on 1 September, this does not give adequate time to provide any response to the consultation. Given the complexity of the models has dramatically increased (i.e. 38 working files versus 8 in GD1) this, combined with the delays, has severely hampered our ability to comprehensively assess and respond even with the use of over 4 consultants full time just on the cost assessment.

IT spend - we are disappointed that the time between BP submission and the DDs was not used more effectively by Ofgem to raise queries in respect of our IT spend. This resulted in a cut of 80% of our Capex IT allowances. Instead we now have to provide significant follow-up evidence in the four weeks between our IT bilateral meeting on 10 August when there were 7 months to deal with this earlier in the year if Ofgem had reached out through the SQ process. Equally, we wrote to Ofgem to say that we would submit this evidence and information by 25 September but there was no positive agreement to this, instead we are being asked to provide this information as early as possible; ideally by 4 September which is extremely challenging.

Refusal to delay response deadline - you'll be aware the ENA ERG requested a two-week extension to the DD response which Ofgem did not approve. Given the multitude of issues mentioned in this response we are disappointed that this was not granted; this represents poor regulatory practice.

Totex cost changes – throughout the DDs there are a number of areas where networks have been asked to consider updating outputs, targets and totex expenditure. We asked the Ofgem cost assessment team how we should provide this information in a consistent format to support the cost assessment process ahead of FDs however we were directed to the individual policy teams. We are concerned that the cost assessment team are not co-ordinating the changes in costs across the GDNs from DDs to FDs and we are unclear how the cost assessment team will consolidate any BP cost changes and appropriately assess costs in order to set the FD allowances. For the avoidance of doubt we plan to submit an updated BPDT Totex worksheet with a walk down to provide fully transparent information for WWU and we would encourage Ofgem to ensure consistency in the way networks provide this information to avoid any misinterpretation in the cost assessment stage ahead of FDs.

In summary, there are a significant number of concerns raised here and we are keen to work with Ofgem to improve the process and ensure the final determinations are robust and that the errors, unnecessary delays and surprises in the FDs are avoided.