

13 August 2021

Our ref: Competition in Connections Review

Kieran Brown
Ofgem
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By email only to: RIIOED2@ofgem.gov.uk

Dear Kieran

Response to Ofgem “*Consultation on the proposal to review competition in the electricity distribution connections market*”.

BUUK welcomes the opportunity to respond to Ofgem’s consultation on the proposal to review competition in the electricity distribution connections market.

BUUK is the parent company of electricity distribution licensees, the Electricity Network Company (“ENC”) and Independent Power Networks Limited (“IPNL”). Our licensees operate as Independent Distribution Network Operators (“IDNOs”), owning and operating ‘last mile’ networks which are principally provided to new developments. Additionally, BUUK is the parent of Power on Connections (“POC”) which operates as an ICP undertaking work which may be adopted by BUUK’s licensees or other distributors.

Operating across all Distribution Services Areas, we engage on a regular basis with all DNOs and also compete with them for the provision and adoption of new connections. We welcomed the competition tests which were undertaken between 2012 and 2014 and worked with Ofgem at the time to provide information and feedback on the competitive environment. We believe that it is right for Ofgem to reassess this now, in order to provide the right incentives for DNOs in the next price control period. In the interim we have worked with DNOs to develop the Competition in Connections Code of Practice (“CiCCoP”) and regularly engaged with DNOs either through forums arranged under the Incentive on Connections Engagement framework or bilaterally where appropriate.

In summary we believe that the approach which Ofgem are taking to measure the level of competition within Relevant Market Segments (“RMS”) is broadly appropriate and will allow for Ofgem to identify the correct incentives which should apply in each of those market segments under RIIO-ED2. We would like to highlight the following points which we believe are particularly relevant when Ofgem considered the competitive environment and sets incentives:

- We believe that Ofgem should undertake a qualitative assessment of the competitive environment in each of the market segments to supplement the quantitative assessment undertaken through the collation of data on the template. This will allow for Ofgem to assess nuances in the underlying competitive conditions in a market segment, properly account for the impact of the COVID-19 pandemic and also provide

an opportunity for parties to consider the future changes of the energy networks which may mean that competition develops differently in the future.

- We believe that DNOs should be incentivised, across the board, on the provision of non-contestable services through the application of the customer service metric. We detail some options for this in our responses to the questions which Ofgem have asked but we believe that the application of Customer Effort Score (“CES”) would be the most appropriate.

We believe that there has been significant divergence between the performance of DNOs in enabling competition and this has been evidenced through their approach to the ICE process and also their delivery of the CiCCoP. We believe that those DNOs who have performed well and where competition is thriving are organisations where senior management has driven the culture to embrace the competitive market and set the tone for DNO employees. We think that it is wholly appropriate for Ofgem to set incentives to encourage this behaviour within DNO organisations through the price control.

We are happy to discuss any of the comments made in this response in more detail with Ofgem.

Yours sincerely

Mike Harding
Regulation Director

Appendix 1 – Responses to Consultation Questions

- 1. Do you agree that the current classification of RMS remains appropriate as a means of distinguishing between different types of connections work and customer type? If you disagree, please provide you views on which alternative classifications should apply.**

We agree that, as of today, the current classification of RMS remains appropriate as a means of distinguishing between different types of connection work and customer type. It may be appropriate in the future to consider the type of equipment being connected to a demand connection (such as EV charging points) as the markets to provide that type of infrastructure may develop differently to the 'traditional' demand connections for commercial or domestic premises. At the moment we do not have evidence of this so believe that the current classification remains appropriate.

- 2. Do you agree with our proposal not to consider the level of effective competition in the excluded market segments? Please provide reasons for you views.**

We agree with this proposal. We are not aware of the development of competition in these areas so do not believe it is relevant to consider the level of effective competition in them.

- 3. Do you agree with our proposal not to consider the level effective competition in the RMS that previously passed the Competition Test? Please provide reasons for your views. Please also provide any information or evidence you have, which may suggest that competitive conditions have materially changed (in particular, if such changes have not been positive) in these RMS since we conducted the Competition Test.**

Whilst we understand Ofgem's position not to consider the level of effective competition in the RMS that previously passed the Competition Test we think that this decision needs to reflect an informed view of the RMS which previously passed the Competition Test such that Ofgem are confident that there have been no negative changes in the conditions of those RMS.

We do not believe that, in the segments in which we compete we have evidence which suggests that the competitive conditions have materially changed. We do, however, believe that there are areas in those market segments where more could be done by DNOs to improve the competitive conditions. We recognise that the competition in connections code of practice has, since the application of the previous competition test, has set a baseline standard that DNOs must adhere to and this baseline prevents regression of segments. However, that baseline standard does not require the DNOs to further develop the competitive environment and we see significant divergence between DNOs on their approach to implementing and administering the requirements under the CiCCoP.

By applying a pass/fail the competition test belies this difference in the competitive environment in RMS which have previously passed the competition tests. Although we agree, in broad terms, that those areas which previously passed the competition test should be excluded (as we haven't seen material changes) we do think that there should be incentives placed on those market segments to improve competition through the enhancement of non-contestable services that DNOs provide. We provide more detail to this in question 9.

- 4. Do you agree with our proposal to assess whether effective competition exists by only considering the key indicators for competition set out in Section 5? Please state why if you disagree, and consider that there are other factors we should take into account, such as DNO behaviour, processes, and customer awareness.**

We agree that the key market indicators in section 5 allow for an assessment of whether competition exists in any given market segment. We do think that this assessment may mask

underlying conditions in the competitive market and the difficulty or barriers to entry which are faced by participants in that market segment. Third party presence and third parties accepting offers for points of connection does not necessarily mean that the environment is capable of supporting competition in the future. Third parties accepting quotes may be loss making because of the high cost to exist in a market segment but may be investing in the future of that market on the basis that a competitive environment will develop. We think that a qualitative assessment of each of the market segments based on feedback from third parties (where such feedback is available) should be used to supplement the key indicators as set out by Ofgem. We would be happy to provide such feedback of each of the segments.

For an RMS that does not pass the competition review, but we consider there to be a prospect of competition developing;

- 5. Do you think we should apply price control incentives on DNO performance? If so, should these be only penalties on poor performance, or should we consider rewarding DNOS that provide a higher quality of service? Please state what impact you consider this might have on competition.**

Yes, we believe that this is an area where we consider price control incentives useful as a mechanism of delivering a competitive environment. We believe such incentives should be limited to the provision of non-contestable services. We go into more detail in our answer to question 9 about how we believe non-contestable services should be incentivised. We think that in areas where competition could develop there should be no incentives for contestable services as to incentivise this would provide an incentive for DNOs over and above the incentives which should be provided by the competitive environment in that segment and this may stifle competition.

- 6. Should we maintain the regulated margin? If you think it should be maintained, please explain why and whether you consider there should be a change in the 4% level of margin that is currently applied.**

Yes, we believe that the regulated margin should be maintained to allow for competition to develop in any areas which fail the competition test and there is prospect of competition developing. We have no evidence to suggest a different level to the existing, 4% margin which we think strikes a balance between protecting consumers and giving head room for competition to develop.

For an RMS that does not pass the competition review, and we consider there to be no prospect of competition developing;

- 7. Do you think we should apply price control incentives on DNO performance? If so, should these just be penalties on poor performance, or should we consider rewarding DNOs that provide a higher quality of service? Please state what impact you consider this might have on competition.**

We believe that in these areas it is important to incentivise DNO performance. In determining the types of incentive and areas to incentivise which are appropriate we think that Ofgem need to be careful to consider why competition is unlikely to develop. We think this is relevant because it is clear that the energy networks are on the verge of undergoing a major revolution and it is possible that, in the future, the services which are not considered competitive today may develop significantly. Whilst it is not clear how these developments may manifest, we think it might be appropriate for Ofgem to set out an incentive framework in this area which allows for the incentives to be agile if it appears that competition may develop in an area where it has previously not been considered.

- 8. Should we remove the regulated margin? If you think it should be maintained, please explain why and whether you consider there should be a change in the 4% level of margin that is currently applied.**

We think that removing the regulated margin in these areas is likely to be in the best interests of consumers subject to the points we raised in answer to question 7 that we think it is possible that the future electricity market may mean competition develops in areas where it is not feasible today. It is important that, in those cases, the regulated margin could be reintroduced as a way of enabling competition to develop.

For an RMS that passes the competition review;

9. Should we limit the application of price control incentives? If you think we should apply price control incentives, please explain what type of incentives would be appropriate.

We think that price control incentives, even in areas which have passed the competition tests, are one of the key areas which Ofgem can ensure the ongoing support of the competitive environment. We think that, in general we would support penalties on poor performance in areas where there is competition, but we would also consider it appropriate for rewards to be applied for a higher quality of service for non-contestable works (which have no prospect of being contestable).

One of the main areas where we currently face issues with some DNOs is in the provision of non-contestable services. This is an area which, in our view, some DNOs have embraced as a genuine service and where we can work with DNOs to resolve issues and the process of working with DNOs is relatively 'easy'. In contrast some DNOs can be difficult to deal with where they provide non-contestable services which are a pillar of the competitive connections environment. That difficulty adds cost and time to third parties to administer the non-contestable process. We believe that in DNO organisations which we see as being easy to deal with it is down, in large part, to senior management and directors buying in to and managing the provision of services. Whilst it might be regretful to come to the position where incentives should be introduced for non-contestable services, we think that the absence of competitive pressure in those areas means that an alternative stimulus is required to drive DNO performance and a price control incentive is likely to be the most appropriate method.

For our own part, we believe that the use of a post service provision metric such as Customer Satisfaction (CSAT), Net Promoter Score (NPS) or Customer Effort Score (CES) calculated through surveys would form a useful mechanism to monitor and incentivise the provision of non-contestable services. Such metrics are easy to administer and require collation of data through surveys to develop quantitative analysis of performance.

10. Should we permit DNOs to charge an unregulated margin? If you think the regulated margin should be maintained, please explain why and whether you consider there should be a change in the 4% level of margin that is currently applied.

Yes, we believe that in this area it is suitable for the DNOs to charge an unregulated margin on the basis that the market will be driven to efficient cost. It is, however, important that DNOs are not able to provide cross subsidies to this cost from other areas of its connections business such that it is able to provide connections at a rate below the market.

11. Do you agree that our assessment criteria successfully capture the key market indicators that would inform us of whether third party presence has expanded or decreased over time? If not, please specify if there is other information we should consider, in determining whether effective competition exists and why.

We agree that the assessment criteria capture the market indicators insofar as the existence of third parties is a strong indicator of the existence of competition. We have noted in answers to previous questions that we believe a qualitative assessment of the level of competition in each of the market segments may be useful to supplement the data and provide Ofgem with a more complete picture about the level of effective competition in each RMS.

The application of the data over a period of time does allow for Ofgem to identify trends in the market which will provide a better view of the level of competition in each RMS and how that segment is, or isn't, developing over time.

12. Should we consider data from the 2020/21 regulatory year or given the impact of the Covid-19 pandemic, would this not be a reliable indication of the underlying levels of competition?

It is true to say that the pandemic may have impacted on the level of competition in the market, but we think that it is important that Ofgem collate this information to understand what that impact is and consider it in the context of the economic conditions.

Where competition had been established or developing in the years preceding the pandemic, we think that the impact of the pandemic may have caused segments of the market to regress and as such the incentives that Ofgem place on those market segments may need to be different to what they would have been had the pandemic not occurred. We don't think that it is appropriate to ignore this data and ignore the impact of the pandemic on competition in market segments.

13. What are your views on the structure of the data template we are proposing to use to carry out our analysis?

We have no comments on the structure of the data template which Ofgem are proposing to use beyond those already made in the answers to other questions.