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Contact / Extension

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By email: RIIOED2@ofgem.gov.uk

Dear Kieran

Consultation on the proposal to review competition in the electricity distribution connections market

SP Energy Networks (SPEN) owns and operates the electricity distribution networks in the Central Belt and South of Scotland (SP Distribution) serving 2 million customers as well as in Merseyside and North Wales (SP Manweb) which serves 1.5 million customers.

We welcome the opportunity to respond to this consultation and support Ofgem undertaking this review of the levels of competition in the connection market. Based on our engagement with Independent Connection Providers (ICPs) and Independent Distribution Network Operators (IDNOs), we believe the introduction of the Competition in Connections Code of Practice has improved the service received by ICPs and IDNOs. As a result, we consider that greater levels of competition have developed within our licence areas since the last evaluation, which took place between 2012-2014. However, we do believe that in order for Ofgem to carry this review out successfully, a number of areas must be clarified, which we have detailed in this response.

Completion and return of Data Templates

Noting the consultation's proposal that DNOs would complete data templates, SPEN would welcome further details on the associated timescales for:

- a) a decision on the proposals within this consultation, including their interactions with existing ED2 timelines, and;
- b) DNOs to complete and submit the data template.

We would also welcome clarity on Ofgem's proposed timelines for 2021/22 connections related regulatory submissions such as the ICE submissions and the Competition Test annual report which is due to be submitted in June 2022.

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The outcome of this competition review will directly impact DNOs' exposure to the new Strategy Delivery Incentive 'Major Connections' within RIIO-ED2. Therefore, understanding the timing of this proposed review, ahead of submitting the final RIIO-ED2 Business Plan on 1st December 2021, is crucial for DNO incentive planning. We therefore call upon Ofgem to undertake this competition review at the earliest opportunity so as to provide clarity to DNOs on incentives, ahead of final Business Plan submission. However, if this competition review is to extend beyond the December deadline, a timetable of works should be developed and agreed with DNOs, at the earliest opportunity.

Evaluation of the Data Provided in the Data Templates

The level of competition within each market segment is determined by the evaluation criteria set by Ofgem. As per Section 5 of the consultation, we understand Ofgem will use 'guiding principles' to determine competition within each Relevant Market Segment (RMS), which could be supported by further information. SPEN requires further information from Ofgem on Ofgem's evaluation process in order to better understand how market segments will be considered to have (1) passed the assessment; (2) have 'a prospect of competition developing'; or (3) have 'no prospect of competition developing'.

It is unclear from the consultation document whether data will be benchmarked across DNOs to define levels of competition. For the avoidance of doubt, SPEN would not support this approach as there will be inherent differences across DNO areas, such as volume of ICPs in operation in a given licence area or prevalence of construction activity, which cannot be fairly compared.

Common Method Statement requirement for Data Templates

We are of the view that a common method statement for completion of the Data Templates is required to ensure that all DNOs complete the templates, using the same methodology. For example, certain elements of the data requested by Ofgem, such as 'Cumulative Total Value (£), includes contestable and non-contestable value figures for full, partial and non-acceptances for DNO and third party' (within Sheet 2,3,4 of the proposed data template). Such a request currently requires an evaluation to be made by DNOs as to what data should be included. In our case, SPEN has a defined method statement as to how the total value of third-party acceptances is quantified. However, we suggest all DNOs should be required to use a common method statement for consistency across the evaluation. We would therefore propose that a common method statement is prepared by Ofgem, with input from the ENA COG Connections Working Group, to ensure that all DNOs fully understand how the data templates should be completed.

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The interdependency between this data and the Major Connections Strategy Delivery Incentive

The proposed competition review mentions specific situations where it may arise that there are 'RMS that did not previously pass the Competition Test and in which we see no prospect of competition developing'. SPEN is keen to understand the criteria for how this would be determined in the context of RIIO-ED2 planning. We understand that according to the Sector Specific Methodology Decision published in December 2020, the Major Connections Strategy Delivery Incentive in ED2 is expected to be symmetrical in terms of exposure, with potential reward in these market segments. Again, it is important that DNOs understand the impact on incentives, in advance of submission of final RIIO-ED2 Business Plans.

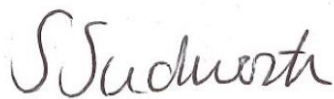
The interdependency between this review and the impact of the Access & Forward-Looking Charges Significant Code Review

The Access SCR is an important review and will likely change customer behaviour due to the change in charging arrangements for reinforcement at the connection boundary. The extent to which this will affect customer behaviour and connection volumes, including in relation to third party works, are likely to only be known once the new arrangements are in place. SPEN recognises the far-reaching impact of Access SCR, particularly on the volume of connection requests, and urge that Ofgem share this perspective and move through this review with caution.

Our full response to those consultation questions, we are best placed to answer, can be found in the enclosed annex.

If you have any further queries relating to our response, please do not hesitate to contact me.

Yours sincerely



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ANNEX

Q1 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 your views on which alternative classifications should apply

SPEN agrees that the current classification of RMS remains appropriate. Changes to the market segments, at this stage, would have a profound impact on RIIO-ED2 planning as well as ongoing reporting. The baseline principles for the Major Connections Incentive are RMS specific, so any changes to these will lead to connections related incentives that are different in size and scope, to those currently planned. For example, SPEN has developed a Connections Strategy, based on the current classification of RMS, to deliver baseline expectations and is based on stakeholder engagement.

Q2 Do you agree with our proposal not to consider the level of effective competition in the Excluded Market Segments?

We agree with the proposals not to consider the level of competition in the Excluded Market Segments. If the proposal was to be expanded, this would impact the scope of the Broader Measure of Customer Satisfaction as well as Time to Connect and the new Major Connections incentive. Significant business planning has already been conducted in these areas in the production of our Draft ED2 Business Plan.

Q3 Do you agree with our proposal not to consider the level of effective competition in the RMS that previously passed the Competition Test?

We are supportive of this proposal as we believe the Code of Practice has continued to develop and improve service for third parties in these segments throughout RIIO-ED1. Therefore, assessment of competition in respect of the RMS that previously passed the Competition Test is unnecessary.

Q4 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.

As per the covering letter to this response, the defining criteria as to what would constitute a 'pass' or 'did not pass' is unclear in this consultation. SPEN would suggest further detail on the assessment criteria outlined in Section 5 is provided for clarity and guidance, in advance of DNOs returning completed data templates. For example, it is unclear if data will be benchmarked across DNOs to define levels of competition. Until this is understood, it is unclear how a multifactor approach will be used to determine the level of competition. For the avoidance of doubt, SPEN would not support a benchmarking approach as there will be inherent differences across DNO areas, such as volume of ICPs in operation in a given licence area or prevalence of construction activity, which cannot be fairly compared.

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

Q6 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.

We understand that 'guiding principles' will be used by Ofgem during this assessment; however, the proposal does not specify the criteria as to how Ofgem will 'consider there to be a prospect of competition developing'. On 18 November 2020 SPEN provided our initial view to Ofgem of the potential output of a rerun of the competition test. We used our own methodology as to how this could be determined. We believe a 4% margin on contestable works allows sufficient headroom for ICPs and IDNOs to compete within the market.

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

Q8 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 understand that 'guiding principles' will be used by Ofgem during this assessment, however, the proposal does not specify the criteria to determine how Ofgem will 'consider there to be no prospect of competition developing'. It is assumed this result could make an RMS eligible for reward, according to the Sector Specific Methodology Consultation and Decision for the new Major Connections incentive. However, it is still unclear how this mechanism will be structured. We do however believe that a 4% margin on contestable works allows sufficient headroom for ICPs and IDNOs to compete within the market.

For an RMS that passes the competition review:

Q9 Should we limit the application of price control incentives? If you think we should apply price control incentives, please explain why and what type of incentives would be appropriate.

As part of the development of our RIIO-ED2 proposals, we have already outlined approaches to the Broad Measure of Customer Satisfaction as well as Time to Connect and the new Major Connections incentive within Chapter Four of our Draft RIIO-ED2 Business Plan. RMS which pass the competition test should provide customers with sufficient choice for completing their works. In addition to this, SPEN has developed a holistic Connections Strategy within our RIIO-ED2 draft Business Plan to improve service for all customers.

Q10 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.

We believe that a 4% margin on contestable works allows sufficient headroom for ICPs and IDNOs to compete within the market.

Q11 Do you agree that our assessment criteria successfully captures 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.

Although the assessment parameters are included in the data template, we require more details to understand the assessment process for how each RMS will be deemed to have 'competition developed', 'prospect of developing' or has 'no prospect of developing'. We would support a common approach across all DNOs as to how data is quantified and returned. We are therefore of the view that a common method statement for completion of the Data Templates is required to ensure that all DNOs complete the templates, using the same methodology. We would therefore propose that a common method statement is prepared by Ofgem, with input from the ENA Connections COG Working Group, to ensure that all DNOs fully understand how the data templates should be completed. As a starting point, we have a detailed approach on our return data which we would be happy to share to facilitate these discussions. A common method statement is particularly important when quantifying the value or 'market share' of third parties.

Q12 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?

Although 2020/21 data is available, if this will be discounted due to a perceived impact of Covid-19, we would suggest not using this data.

Q13 What are your views on the structure of the data template we are proposing to use to carry out our analysis?

The data template does not seem to allow for the inclusion of projects which were quoted and paid for in different regulatory years. This will result in material changes to the value data of the returns and the potential non-inclusion of valid transactions. Given that the current validity of quotations can be between 3-6 months, this is an important parameter we would ask to be included in the data template.

As per our response to Q11 (above), we would support a common approach to how data is quantified and returned across all DNOs. We have a detailed approach on our return data which can be shared for approval.