

Ofgem proposal to review competition in the electricity connections market for RIIO-ED2

WPD consultation response - 12 August 2021

THE PROPOSED SCOPE OF THE REVIEW	
<p>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</p>	<p>We agree - The Relevant Market Segments are well established and have shown to work effectively over the last eleven years. We are aware that the CSVc working group reviewed the ongoing applicability of the RMSs in their current form and discussed whether it would be more appropriate to categorise by customer segment (e.g. developer or local authority) instead of connection segment or to measure by market type such as low carbon technology. While there may be some benefit to this approach the case is not overwhelming and, for the purposes of undertaking this review, it makes sense to request data based upon recognised customer segments.</p>
<p>Q2. Do you agree with our proposal not to consider the level of effective competition in the Excluded Market Segments? Please provide reasons for your views.</p>	<p>We agree - whilst there are signs of emerging competition in excluded market segments (LVSSA/LVSSB), ICP activity in this specific area still remains low therefore it is likely that any review would show that competition is yet to be sufficiently developed as to warrant opening these markets up.</p>
<p>Q3. Do you agree with our proposal not to consider the level of effective competition in the RMS that previously passed the Competition Test? Please provide reasons for your views. Please also provide any information or evidence that 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.</p>	<p>We agree. WPD passed thirteen of thirty-six market segments across its four licence areas, predominantly in the unmetered and metered demand HV and EHV sectors. Evidence clearly suggests that competition has remained steady and in some cases increased since the Competition Tests were originally run. ICPs continue to undertake the majority of unmetered new connections and transfers. We have also seen an increase in the number of IDNOs who are active in our areas (now thirteen), particularly in the housing sector. Allowing the ICP to determine the point of connection to the existing network is just one example of how the industry has worked together since the Competition Test was run to open up the competitive market. When considered in the round we believe there is nothing to support any proposal to consider the level of effective competition in the RMS that previously passed the Competition Test.</p>

THE PROPOSED SCOPE OF THE REVIEW - continued	
<p>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.</p>	<p>We welcome Ofgem's intention to allow supplementary information to be submitted as part of the assessment. We believe assessment through a combination of the Legal Requirements Test and the submission by the DNO of information via the proposed data template is an appropriate means of identifying if effective competition exists. We believe that the proposed key market areas for assessment, when considered in unison, will serve to indicate the level of penetration in each market segment. There is however, a strong case to draw on any evidence provided by other means as the key market indicators may not provide a complete picture. For example, the proposed data template does not require the number of metered connections made by DNOs and third parties. The domestic market is heavily dominated by IDNOs, but a straightforward analysis of connection capacity, particularly at HV and HV/EHV might not bring this out. DNOs may be able to provide an estimate of the number of connection made in this respect.</p>

POSSIBLE OUTCOMES FROM OUR REVIEW OF COMPETITION	
For an RMS that does not pass the competition review, but we consider there to be a prospect of competition developing;	
<p>Q5. 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.</p>	<p>We support placing incentives on DNOs as this will ensure that they focus on improving services in areas where competition is less effective. Rewards for providing higher quality service may incentivise DNOs to go above and beyond what they might do under a penalty system only and it makes sense to encourage DNOs to be ambitious in their approach. Any potential for reward however, must be allowed only through a CVP that demonstrates the additional value its plan will generate for consumers. Well justified CVPs could be used to help establish the standards against which performance of all DNOs is measured. We note Ofgem's concerns that rewarding DNOs could distort competition in the market but we think the welfare of the end consumer is of paramount importance.</p>
<p>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.</p>	<p>We support maintaining the regulated margin at 4% as an appropriate level. The additional cost of work for competition to develop will be negligible in terms of overall expenditure as DNOs seek to make improvements through efficiencies therefore consumers should not see an increase. We agree that removal of the regulated margin would not help competition to develop.</p>
For an RMS that does not pass the competition review, and we consider there to be no prospect of competition developing;	
<p>Q7. 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.</p>	<p>Yes. We believe a similar approach as described in Q5 is appropriate. Incentives should apply where there is no prospect of competition developing although a balance needs to be found between the 'carrot and the stick' approach. DNOs should be held to account where they do not deliver in areas where there is little or no competition but rewards could incentivise DNOs to consider more innovative ways of opening up competition.</p>

POSSIBLE OUTCOMES FROM OUR REVIEW OF COMPETITION - continued	
<p>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.</p>	<p>We do not support the removal of the regulated margin. While we understand there is an argument to remove the regulated margin where there is no prospect of competition developing we believe that in many instances there is potential to develop competition through innovative means, therefore the focus should be on incentivising DNOs to continue to explore means of opening up these areas. As a consequence, there is no compelling case to remove the regulated margin.</p>
<p>For an RMS that passes the competition review;</p>	
<p>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.</p>	<p>We agree that it is entirely appropriate to limit the application of price control linked incentives in RIIO-ED2 for those RMS that pass the competition review. This is consistent with the current approach under RIIO-ED1. While the Major Connections Strategy will only apply to RMS that have not passed the Competition Test, DNOs generally take a holistic approach to the delivery of customer service and recognise that reputational value is just as important. There is little advantage for example in neglecting one area of unmetered connections that has passed the Competition Test when looking to make improvements in another unmetered RMS that has not. We also note that it is Ofgem's intention to ensure that, in order for DNOs deliver best practice in the provision of non-contestable activities, their strategies should capture these activities, even where these have passed the Competition Test. This will provide further protection for the consumer.</p>
<p>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.</p>	<p>We support a continuation of unregulated margins for RMS that have passed the competition test. DNOs should be able to respond to market signals in these RMS. A fixed margin would be a distortion. We believe that, in the interests of consistency and due to the lack of evidence to suggest otherwise, DNOs should be able to charge an unregulated margin on those RMSs that pass the competition review.</p>

PROPOSED APPROACH TO REVIEWING POLICY	
<p>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.</p>	<p>The key market indicators, when considered in the round, do enable an assessment of the level of market penetration in competition. However, there are two factors that need to be considered. Firstly, as this information only covers the last three regulatory years it is arguable that it is not entirely reflective of changes that have occurred in the interim period after the original Competition Test was undertaken and leading up to this point. Market penetration may have plateaued to an extent over the last three regulatory years and so this may not provide a totally accurate representation of whether third party presence has expanded or decreased over time but could demonstrate a stable market. We are not necessarily advocating that the review should look further back and only seek to raise awareness that taking data from the last three regulatory years may not provide the entire picture. Secondly, whilst a strong indication of an active market in terms of offers issued, DNOs are not the main factor impacting the number of third parties accepting schemes – this is more influenced by the competition between third parties. We therefore consider the number of third parties accepting offers should have a much lower weighting than the overall share between DNO and (total) third parties, in the assessment.</p>
<p>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?</p>	<p>We support the inclusion of data from 2020/21 for completeness although it is possible that some results may be affected. Where the DNO believe this to be the case they should have the opportunity to highlight and comment on any perceived anomaly.</p>
<p>Q13. What are your views on the structure of the data template we are proposing to use to carry out our analysis?</p>	<p>The structure of the data template will broadly deliver the key market indicator information that Ofgem propose to use for their analysis. However, we believe that more comprehensive and intuitive guidance is required at the time the template is issued in order to provide complete clarity and detail concerning the data required. This will ensure that DNOs are consistent in their approach to completing the template.</p>