

→ Karl A. David H



SP Transmission & Distribution

Maxine Frerk
Director, Coordination and Metering
Office of Gas and Electricity Markets
9 Millbank
LONDON
SW1P 3GE

Your ref
Our ref
Date
22 August 2003
Contact/Extension
01698413476



Dear Maxine,

ELECTRICITY DISTRIBUTION PRICE CONTROL REVIEW - METERING ISSUES

INITIAL CONSULTATION - JULY 2003

SP TRANSMISSION & DISTRIBUTION RESPONSE

Thank you for the opportunity to comment on your initial consultation on metering issues associated with the distribution price control review.

A concern with the document is that it focuses on the mechanics of a possible price control without clearly defining the DNO's ongoing obligations in respect of metering services. It is imperative that these ongoing obligations are agreed as a matter of urgency as only then is it appropriate to enter into detailed discussion on the form of any price control. In particular, Ofgem should recognise the developments in the provision of Meter Maintenance Services (MOp) and give a clear direction that this obligation will transfer back to suppliers from 1st April 2005 and no longer be subject to price control.

We do not accept the conclusions that a separate price control is required and the approach outlined below is more appropriate in delivering the required objectives:-

- a) MOp to be transferred back to suppliers and not subject to any price controls.*
- b) New meters to be provided on a competitive basis and subject to normal competition rules and not subject to any price controls.*
- c) Existing meters to be covered as part of the allowed revenue under the distribution control but with appropriate adjustments to allowed revenues should metering assets be sold. The concerns regarding cross-subsidy should be addressed by DNO's demonstrating to Ofgem that their charges are based*

Members of the ScottishPower group

New Alderston House Dove Wynd Strathclyde Business Park Bellshill ML4 3FF
Telephone (01698) 413000 Fax (01698) 413053

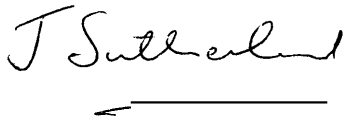
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on the modern equivalent asset value, the life of the meter and an appropriate cost of capital.

We still support the position set out by all DNO's in the meetings with Richard Ramsey in October 2002 and with Martin Crouch in May 2003. We are concerned that the DNO proposal was dismissed in the consultation paper without proper consideration. The DNO proposal meets the key requirements set out by Ofgem and in a more simplified manner.

Our full response to the consultation is attached which includes our views on future DNO obligations and the correct price control mechanism to support these obligations.

Yours sincerely

A handwritten signature in cursive script that reads "J Sutherland". Below the signature is a horizontal line with a small arrowhead pointing to the left.

Jim Sutherland
Asset Director

ELECTRICITY DISTRIBUTION PRICE CONTROL REVIEW - METERING ISSUES: INITIAL CONSULTATION JULY 2003

RESPONSE BY SP TRANSMISSION & DISTRIBUTION

1. DNO OBLIGATIONS

- 1.1 The most fundamental metering issue for the coming price control is the nature of the continued obligations of DNOs to provide metering services in a competitive metering market. There is insufficient discussion of this in the document and this key issue requires resolution before an informed view on the form and duration of the price control can be taken.
- 1.2 Meter Asset Provision (MAP) and Meter Maintenance (MOp) were previously made DNO obligations as part of a combined Meter Operation Service as the DNOs owned the metering assets. Meter Reading, Data Processing and Data Aggregation were made supplier responsibilities. Now the MAP and MOp services have been separated as part of the REMA process, it is essential that DNO obligations are revisited. The MOp service is primarily labour provision and is closely linked to Meter Reading. British Gas Trading have already appointed their own service provider for MOp services and it is known that other major suppliers are looking to do the same. A continued obligation on DNOs to retain the capability to provide a MOp service where requested will require DNO's to retain significant fixed costs. This is inefficient and fails to recognise the rapid development of the market for MOp services. It is therefore appropriate to end the current licence requirement that suppliers' statutory obligation to provide and maintain meters should be underwritten by DNOs on demand.
- 1.3 An early recognition by Ofgem that the MOp service should be transferred back to suppliers is essential and will allow the discussion in the Price Control Review to focus on metering assets. This is recognised in the paper in that the MOp service, which accounts for approximately one third of metering revenues is barely mentioned as the issues are primarily associated with metering assets.
- 1.4 It is accepted that some continued obligation on DNOs in respect of MAP services for existing metering is required in the short term. ***This DNO obligation for MAP should be limited to the provision of existing DNO metering assets, situated in customers' premises. It should not be obliged to offer MAP services once the meter is removed.***

2. METERING CONTROLS

- 2.1 The paper fails to take sufficient account of the nature of the metering market. Metering services are almost entirely provided to suppliers who have significant market power to obtain the services they require at prices they are prepared to pay. If they obtain services at too high a price and try to pass these onto customers then the competitive supply market will protect end customers.

2.2 Retaining the MAP service for new installations within the Price Control will, by definition, inhibit the development of new technology which Ofgem state (in paragraph 3.15) as a key objective. New technologies could help suppliers reduce costs in other areas of their value chain for which they would be prepared to pay a premium. Ofgem recognise this fact in paragraph 6.33 by proposing that any price control should be limited to 'basic' meters. However, this also needs to be reflected in a modification to the DNO's Licence obligations in respect of MAP.

2.3 *We do not accept the conclusions that a separate price control is required and we consider that a better regime is outlined below, which is expanded upon in section 4 of our response:-*

- a) MOp (as discussed previously) to be transferred back to suppliers and not subject to any price controls.*
- b) New meters to be provided on a competitive basis and subject to normal competition rules and not subject to any price controls.*
- c) Existing meters to be covered as part of the allowed revenue under the distribution control but with appropriate adjustments to allowed revenues should metering assets be sold. The concerns regarding cross-subsidy should be addressed by DNOs demonstrating to Ofgem that their charges are based on the modern equivalent asset value, the life of the meter and an appropriate cost of capital (recognising the additional risks due to early removal of assets).*

3. VALUATION OF METERING ASSETS

3.1 We recognise that it is important that a method for determining the Metering RAV should be established in order to determine the adjustment to distribution allowed revenues should a DNO sell some or all of its existing metering assets and hence remove or reduce any continued obligations to provide the service. We support the proposal suggested in paragraph 5.3 to use a depreciated replacement cost basis as this is most likely to promote competition and will not restrict the sale of metering assets.

3.2 We therefore support the general conclusions set out in paragraph 5.5 but this should be used to adjust distribution revenues in the event of the disposal of metering assets and not to set a new metering price control. Any dispute over charging for existing metering will continue to be subject to determination by the Authority. This and competition law should be sufficient to address any concerns over future metering charges.

4. STRUCTURE OF THE PRICE CONTROL

4.1 As stated previously, we do not support a separate metering price control but recognise that the continued obligations on DNOs to provide existing metering should remain within the remit of the distribution price control. This should exclude half-hourly metering and larger commercial sites where current-transformer operated meters are installed.

- 4.2 Our rationale for excluding **MOp** services has been detailed earlier and is due to the way competition is already developing and the similarity of this service to meter reading, which is already a supplier activity and not subject to price control. In relation to the provision of MAP services, whilst competition may not be sufficiently developed today, this is primarily due to the fact that the REMA separation only came into effect on 29th May 2003. Competition will be introduced for British Gas customers when meters require changing for certification purposes, and hence DNO's market share will start to reduce. The DNO role in MAP is now restricted to purchasing meters from manufacturers and then leasing them to primarily suppliers. DNOs add very little value to this process which could be provided directly by manufacturers or alternatively through financial institutions.
- 4.3 The Distribution Price Control should be set on the basis of the MAP service for existing metering assets and no new metering investment by DNOs coupled with ending of the obligation to provide the **MOp** service. If DNOs invest in new meters it should be on a commercial basis and any income treated as unregulated. Where a DNO disposes of its metering assets (either in bulk or to individual suppliers or service providers) allowed revenues should be reduced based on the Depreciated Replacement Cost of the assets sold. This is not an ad hoc adjustment as suggested in paragraph 4.16 of the consultation paper.
- 4.4 In order to send the correct message to the market to avoid unnecessary metering changes and provide DNOs with a degree of protection from asset stranding, DNOs should be able to charge termination payments where a meter is removed before the end of its life where this is not due to a metering fault. This approach will ensure meters are only removed where there is a valid justification, for example where a supplier wishes to adopt an automatic meter reading system. This approach addresses the concerns raised by Ofgem in paragraph 4.13 regarding protection of recent assets whilst going some way to address the DNO's concerns.
- 4.5 In response to the specific questions set out in the paper, the scope of any price control should be restricted to MAP and the DNO's existing assets (excluding half-hourly and larger commercial meters); the form of the price control should be as set out above and the timescale should be for the period of the next distribution price control or until the DNO disposes of its existing assets, whichever is the shorter.
- 4.6 To ensure DNOs do not cross-subsidise their MAP activities, Ofgem should be able to review the charges in accordance with paragraph 2.3(c) above.
- 4.7 The above approach satisfies the objectives set out by Ofgem without the complexity of a separate metering control and recognises the current reality of competition in metering services.