

**Response from Western Power Distribution (South West) plc and  
Western Power Distribution (South Wales) plc**

**Electricity Distribution Price Control Review, Policy document, March 2004**

**EXECUTIVE SUMMARY**

**CHAPTER 3. Form, structure and scope of the price controls**

We believe that RPI is a better indicator than CPI of changes to our underlying costs and should therefore be retained in the price control post April 2005

The introduction of standards of performance across all new connections should not be pursued unless there is clear, verifiable evidence for their need

WPD has and will continue to put considerable time and resource into minimising the rateable value proposals of the Valuations Office Agency for WPD South West and WPD South Wales

We agree with the proposal to include EHV charges within the scope of the price control as this will reduce any incentives to treat EHV customer charges differently to other customers We believe it would be better to align the treatment of top up and standby with that of EHV revenues

The distinction between opex and capex should be preserved and indeed strengthened by the use of more prescriptive definitions

The only way of addressing companies submitting inflated capex forecasts is to consistently model network replacement needs company by company on the same replacement criteria. Companies would then have to justify particular characteristics of their network to justify any deviation from these assumptions

DNOs should be able to recover all costs, both capital and operating, that they have incurred in providing metering services in order to meet their historic and future licence obligations

For MOP services price caps supported by non-discrimination provisions are preferable to an average revenue cap

**Chapter 4. Quality of service and other outputs**

Our initial view is that the arrangements applicable during severe weather conditions should be included in a modified version of the arrangements that were introduced in October 2003

We agree with the principle that the most appropriate means of addressing the perverse incentives associated with the deferment of planned works during 2004/05, would be to allow companies to “roll forward” a proportion of their planned interruption performance from 2004/05 into 2005/06. However, we do not agree with the details of Ofgem’s proposal.

We agree with Ofgem’s proposal that, as an alternative to the existing multiple interruption Overall Standard, the reporting of the number of customers experiencing particular frequencies of interruption each year should be integrated into the IIP reporting framework

It would be appropriate to maintain the current level of financial exposure in respect of IIP. The annual settlement of rewards and penalties would have stronger incentive properties than a five yearly settlement arrangement.

We suggest that a total annual reward of £1m would provide sufficient improvement incentive. We propose that the discretionary award should be assessed across a range of performance criteria.

#### **Chapter 5. Distributed generation, innovation funding and registered power zones**

Whilst agreeing that the costs of connecting generation should be recovered from generation connections, we remain concerned that the incentive rate will cease should a generator terminate their connection. This is likely to lead us to consider the application of termination charges (to cover non pass through costs) to generators that will need a form of financial guarantee similar to that applied to generation connections by NGT.

Whilst agreeing with the objectives of the IFI scheme, it is unlikely to have any significant influence on the level of funding of research but will significantly increase the administrative burden associated with it.

Whilst agreeing with the objectives of RPZs, there is still a significant administrative burden and risk left with the distributor compared to the level of reward proposed.

#### **Chapter 6. Assessing costs**

DNOs can achieve head office and corporate cost savings through being part of a larger group; such savings should be taken into account when comparing DNOs for the purposes of benchmarking

#### **Chapter 7. Financial issues**

WPD welcomes the introduction of the Special Administration regime and the clarification of the financial ring-fence set out in paragraphs 7.7 to 7.16

WPD's reaffirms its agreement with Ofgem's principle that recognition of pension costs associated with regulated distribution and metering activities should be included in the allowed income for DNO's

WPD support Ofgem's view that the liability relating to active members be allocated according to their present employment

WPD supports Ofgem's approach to allocate pre-privatisation leavers based on the employment costs in the year of privatisation

In relation to Early Retirement Deficiency Costs, we continue to strongly disagree with Ofgem's view that companies should be penalised for not making payments into the scheme at the time it was in surplus

Finally WPD notes that Ofgem may be thinking of applying a fixed allowance for future service costs. We would strongly oppose this approach as the characteristics of ESPS groups make the approach unreasonable

**Response from Western Power Distribution (South West) plc and  
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**Chapter 3. Form, structure and scope of the price controls**

**Price Index**

Para 3.14 – We believe that RPI is a better indicator than CPI of changes to our underlying costs and should therefore be retained in the price control post April 2005.

**Voluntary standards of performance**

Para 3.39 - In seeking to extend voluntary standards of performance to all new connections it is important to consider the following;

- Is there a real and verifiable problem with existing performance ?
- Housing and street lighting work is generally straightforward, but other connections can be far more network interactive, requiring complex studies, sometimes multi-party.
- Larger schemes are more likely to involve requirements for external consents such as, planning and environmental consents, Traffic Management Bill programme imposition etc. timescales for which are outside DNO control.

Consequently the introduction of standards of performance across all new connections should not be pursued unless there is clear, verifiable evidence for their need, across each connection type and voltage, and then meaningful standards are capable of being developed for each having regards to external variabilities and time drivers.

**Ofgem proposes that the treatment of units distributed to embedded networks should be consistent with that for wheeled units, i.e. included within the scope of the price control.**

Para 3.42 – Aligning the treatment of units exported to embedded networks with that of wheeled units is appropriate and consistent with avoiding the creation of perverse incentives.

Para 3.43 - WPD has and will continue to put considerable time and resource into minimising the rateable value proposals of the Valuations Office Agency for WPD South West and WPD South Wales

**Views are particularly invited on the:**

- **weighting of EHV units in the revenue driver:**

Para 3.30/3.41 – We agree with the proposal to include EHV charges within the scope of the price control as this will reduce any incentives to treat EHV customer charges differently to other customers. However the proposal to continue to exclude top up and standby charges will leave a distortion because many EHV customers have on-site generation that runs in parallel with our network. We believe it would be better to align the treatment of top up and standby with that of EHV revenues i.e. to price control those that already exist and to treat any new ones during the next price control period as excluded. We believe that this treatment of top up and standby is essential if the policy intention of EHV customers being treated on an equal footing to other customers is to be achieved.

- **treatment of DNOs' out of area networks:**
- **definition of costs:**

**3.61 Definition of costs and incentives**

The distinction between opex and capex should be preserved and indeed strengthened by the use of more prescriptive definitions. We recognise that the determination of definitions is difficult, but it is essential that the expertise and understanding developed in the current review is captured to develop such definitions for the next review period

It is important that capex additions are defined so that the RAV is then a easily calculable number. The RAV is widely accepted as representing the economic value of the network and is a critical measure of value used by rating agencies, bondholders and other interested parties.

Differing practices adopted by companies in accounting for overheads and faults significantly distort the opex/capex boundary. We note Ofgem are putting considerable resource into resolving these distortions but realistically do not consider that the fault boundary issue will be adequately resolved for this price review settlement.

WPD proposed a definition of faults to Ofgem in May 2002, that we have applied in 2002/03. This definition in essence is that a fault is due to network failure whether as a result of weather or as a result of failure of materials (e.g. a pole collapses). Subsequent work arising from the fault that:

- replaces part of the network i.e physical faults; the expenditure thereon should be capitalised and categorised as “capitalised faults”
- involves no replacement i.e. non-physical faults; the expenditure thereon should be expensed and categorised as “expensed faults”

WPD believes this distinction could be applied in the future by Ofgem to derive consistency. However, we recognise that this now will probably be unachievable for the current review.

We therefore propose that Ofgem focus on ensuring that total fault costs are captured by all DNOs based on a consistent definition of what constitutes “fault costs”. Ofgem would then be in a position to determine the extent to which these costs are treated as opex. ; We would support a decision to treat 50% as opex as an interim solution for the next review period

○ **incentives for investment underspend, including practical ways of linking capex incentives with outputs and taking account of differences in capex forecasts across companies; and**

Para 3.65 – The only way of addressing companies submitting inflated forecasts is to consistently model network replacement needs company by company on the same replacement criteria. Companies would then have to justify particular characteristics of their network to justify any deviation from these assumptions.

Companies should be asked to re-consider their investment forecasts. Then for the next review period, Ofgem should adopt a banding approach:

- 0% to 10% underspend: Retain return and depreciation for five years
- 11% to 20% underspend: Retain return only for five years
- 21% to 30% underspend: Retain nothing
- 31% and above: Penalty imposed

Para 3.66 – If capex needs are assessed on the basis described above, then IIP would continue to be the appropriate place to incentivise and reward outputs.

Para 3.67 – Treatment of capex overspends We do not agree with the middle statement of partial recovery for investment in a ‘middle ground’. For example, the investment made in removing D Poles from the network in S Wales is a significant contributor to the overspend on investment. The October 2002 storm demonstrated, with hindsight, the value of this investment in customer service, but under the proposed criteria we would not have received the regulatory depreciation for a 5 year period on this spend. There should only be the two criteria and the distributor should justify it’s spending during the price control review process.

## **Losses**

The inclusion of losses associated with EHV consumption introduces additional volatility that is outside the control of the DNO.

- **the approach to metering.**

## **Stranding**

Para 3.84 – 3.85 DNOs should be able to recover all costs, both capital and operating, that they have incurred in providing metering services in order to meet their historic and future licence obligations.

This is not a matter of ‘protection’. DNOs have not had a choice or made an independent commercial decision to incur expenditure to meet licence obligations. It is a matter of principle and trust that, within a regulated licensed environment, the efficient costs of meeting licence obligations should be fully recoverable and that the rules should not be changed retrospectively.

## **Form of Price Control**

Para 3.92, 3.96 - For MOP services price caps supported by non-discrimination provisions are preferable to an average revenue cap approach for the following reasons:

- a price cap approach would result in cost based service prices that are informative in the marketplace and therefore support the development of competition. An average revenue cap does not, in itself, regulate prices.
- a price cap approach does not require a mechanism for dealing with over or under recovery. An average revenue cap would require such a mechanism, which would result in the distortion of prices away from being cost reflective and informative.

For an average revenue cap to work, the number of drivers must reflect the variability of services to avoid the possibility of efficient costs not being recoverable. To keep the number of drivers manageable, the average revenue cap should be limited to the provision of basic metering services only (see below), with all other prices or price differentials being excluded. For example, MOP services are available for differing notice periods with the price varying inversely to the length of notice; the basic metering service would be for the standard notice period, which attracts the lowest price; shorter notice periods would attract a price differential that would be excluded for the revenue cap.

The number of visits would be the logical base driver, but subdivision by customer type is not logical. This is because customers of different types can have the same metering equipment installed and it is the type of metering equipment and therefore the time on site that determines MOP costs and should therefore drive revenue. A more logical subdivision by equipment type would be single-phase credit, single phase pre-payment, poly-phase, maximum demand and current transformer. There would also need to be a driver for visits where no meter is installed to cover e.g customer service or read and re-set visits. This would result in 6 drivers, which is a manageable number and could cope with variations in volumes and mix.

### **Basic Metering Service**

Para 3.97 – 3.101 - The definition of a basic meter service is broader than the meter type (Para 3.99, 3.100). This is important for both MAP and MOP. The scope of the service itself needs to be defined in addition.

For example, it needs to be clear that MAP is an “over the counter” service and does not include delivery. Other matters need to be explicit also, such as rental period, warranties and how early return is accounted for. Without these and other aspects being clearly defined, pricing is not transparent. Clarity ensures that both the service provider and customer understand what to expect for the price.

Similarly, in MOP the basic service needs to reflect such things as service periods, notice periods, volume limitations and materials content as well as the core service description.

All this will need to be reflected in individual service contracts so that there is no doubt what charges are included in the price control and what is excluded. This is currently dealt with through the JPW contracts with standard terms and conditions, although they currently cover a broader range than a basic metering service. It is not possible to set prices for services without a clear understanding of the terms and conditions that apply to their provision.

This potential complexity can be better addressed through a price cap approach, with prices given for a small number of clearly defined services, combined with a non-discrimination provision. With an average revenue cap approach based on the basic metering service, neither Ofgem nor we are in control of the demand for those services. Suppliers will determine whether they want the basic metering service or something outside those constraints. Consequently, it is possible that few services are delivered within the context of the “basic metering service” and the majority of services could become excluded with the only means of control being through ex-post regulation.



## **Chapter 4. Quality of service and other outputs**

Guaranteed and Overall Standards of Performance (GOSPs)

### **Guaranteed standard on supply restoration**

Our initial view is that the arrangements applicable during severe weather conditions should be included in a modified version of the arrangements that were introduced in October 2003.

### **Automatic payments**

In respect of failure to deliver the Guaranteed Standard for supply restoration during normal weather conditions it would be appropriate to:

- Introduce a “semi-automatic” arrangement for the payment of compensation to customers; and
- Introduce an equivalent penalty where compensation payments are not made to customers.

It would not be appropriate to introduce either automatic or semi automatic payments for:

- Failure to achieve target supply restoration targets during severe weather conditions; and
- The multiple interruption and planned interruption Guaranteed Standards.

### **Compensation for business customers**

For business customers connected at HV and above, the compensation arrangements should be considered in the light of the results of a willingness to pay survey specifically targeted at this customer group. The compensation arrangements should also recognise that existing networks have been designed and are operated in accordance with Engineering Recommendation P2/5: Security of Supply.

### **Priority Service Customers**

There would be merit in establishing a dedicated contact line for priority service customers in order to facilitate the provision of our obligations in respect of vulnerable customers.

## **Multiple Interruption Guaranteed Standard**

The Guaranteed Standard for multiple interruptions has been operational for two full years. Customer research has identified that there is currently a low level of knowledge of this Guaranteed Standard amongst customers.

In our narrative response to the Forecast Business Plan Questionnaire, we outlined the implications of a tightening of the multiple interruption Guaranteed Standard. The added customer benefits of tightening the Guaranteed Standard do not justify the added costs.

## **Reviewing the Information & Incentive Project (IIP) Provision of Disaggregated Interruption Data**

The HV circuit data should be used for comparing quality of supply performance and for developing overall quality of supply targets. However, it would not be appropriate currently to use the HV circuit data to set disaggregated performance targets.

## **Supply Restoration Duration Bands**

The output should report the number of customers interrupted within duration bands integrated into the IIP framework should:

- Include interruptions due to unplanned incidents on the DNOs own network only;
- Exclude re-interruptions of supply; and
- Be disaggregated by voltage level in order to provide more meaningful inter DNO comparison.

It would not be appropriate currently to introduce performance targets for this output measure.

## **Worst Served Customers**

We agree with Ofgem's proposal that, as an alternative to the existing multiple interruption Overall Standard, the reporting of the number of customers experiencing particular frequencies of interruption each year should be integrated into the IIP reporting framework. We recommend that the reported output should:

- Include interruptions due to unplanned incidents on the DNOs own HV, EHV and 132 kV networks only;
- Exclude re-interruptions of supply; and
- Exclude short interruptions.

It would not be appropriate currently to introduce performance targets for this output measure.

## **Connections**

We agree with Ofgem's proposal to transfer the existing Overall Standard for connections reporting requirements into the IIP reporting framework.

## **Form of the Incentive Scheme**

It would be appropriate to maintain the current level of financial exposure.

In respect of incentives for network resilience, Ofgem propose to differentiate between small severe weather events and large severe weather events. In order to prevent the potential penalising of a company within both the quality of service and network resilience incentive schemes for a single small severe weather event, it will be necessary to re-define the exclusion criteria, with the objective of ensuring that all small severe weather events are excluded from the quality of service incentive scheme.

The annual settlement of rewards and penalties would have stronger incentive properties than a five yearly settlement arrangement.

## **Weighting of Planned and Unplanned Interruptions**

It would be appropriate to derive separate assumptions for the number of planned and unplanned interruptions, but to combine those assumptions into a single quality of service target for the number of interruptions.

The same approach should be adopted for the duration of interruptions.

## **Audits and Adjusting Data for Inaccuracy**

By now each company will have experienced two full IIP audits. These audits have identified:

- Small reporting inconsistencies across companies; and
- Overall reporting accuracies ranging from 95.7% to 99.6%.

The objectives must be to eliminate any further reporting inconsistencies and to level up the reporting accuracy.

In considering the two options for the IIP audit framework for the next price control period, we recommend that a “streamlined version” of the existing audit should be adopted. This will facilitate the driving out of any residual reporting inconsistencies.

We do not support Ofgem’s proposal that, in the next price control period, performance data should always be adjusted for any inaccuracies identified in audits. We propose that a tightening of the accuracy requirement would be more appropriate

Once the residual reporting inconsistencies have been driven out and reporting accuracy has been levelled up, it would be appropriate to require companies to undertake the annual audits, with Ofgem carrying out random verification checks.

The penalising of companies if their reported data failed to meet the accuracy requirement, should only be a consideration once reporting inconsistencies have been eliminated and reporting accuracy has been levelled up.

### **Treatment of Planned Interruptions for the Final Year of This Price Control Period**

We agree with the principle that the most appropriate means of addressing the perverse incentives associated with the deferment of planned works during 2004/05, would be to allow companies to “roll forward” a proportion of their planned interruption performance from 2004/05 into 2005/06. However, we do not agree with the details of Ofgem’s proposal.

We propose a more robust and challenging arrangement whereby:

- Those requesting roll forward should notify Ofgem by 30<sup>th</sup> April 2006;
- Only companies who Ofgem deem to be frontier performers would be permitted to exercise the roll forward option; and
- A company should be permitted to roll forward an amount, of both planned Customers Interrupted per 100 Customers and Minutes Lost per Customer, that can be fully justified by the company as work that could have been deferred and verified subsequently by Ofgem.

### **Frontier Performance**

We propose that:

- The identification of the best performing companies should be undertaken by comparing each company’s actual performance with their benchmark performance and then ranking the relative performance;
- Benchmark performance for each company should be determined using disaggregated (normalised) network performance data; and
- If a company is identified as a best performer for one of the output measures, then that company should be eligible to participate in the reward mechanism for both output measures.

### **Network Resilience**

In respect of the ability of a company to restore supplies following severe weather it is essential to differentiate between:

- Compensation payments to customers (or equivalent reduction in allowed revenue);
- Mechanisms for the recovery of compensation payments;
- Rewarding of company performance; and
- Treatment of repair costs associated with severe weather events.

## **Compensation Payments to Customers (or Equivalent Reduction in Allowed Revenue)**

We agree, in principle, with Ofgem's initial proposals that the interim arrangements introduced in October 2003, should be refined to cater for:

- No severe weather;
- Smaller severe weather events;
- Large severe weather events; and
- Very large severe weather events.

There are interdependencies between the definitions of severe weather events; the IIP exclusion criteria and the trigger periods for customer compensation payments. Until these interdependencies have been analysed, it is not possible to provide substantive comment regarding the suggested trigger periods for both smaller and larger severe weather events. We propose that the Ofgem Quality of Supply Working Group should undertake the required analysis.

## **Mechanisms for the Recovery of Compensation Payments**

We propose that a proportion of the compensation payments, to customers affected by both smaller and larger severe weather events, should be a pass through cost. It would be appropriate to use a sliding scale cost recovery profile. Due to the interdependency of this issue with other factors, such as the trigger period for compensation payments, we propose that the Ofgem Quality of Supply Working Group should give consideration to the cost recovery profile and mechanism.

## **Rewarding of Company Performance**

With a mechanistic approach to the payment of customer compensation and cost recovery, there is the potential that a company could be penalised financially, yet that company had actually performed extremely well. This would not be appropriate. We propose that an incentive mechanism should be introduced whereby companies are rewarded for good performance during severe weather events. This would require an ex-post evaluation of a company's performance across a number of criteria including mitigating actions, mobilisation of resources, communications etc.

## **Capping Exposure and Payments**

We propose that, in line with the existing interim arrangements:

- The cost of compensation payments to customers should be subject to an annual cap of 1% of base price control revenue; and
- The maximum payment to a customer should be £200.

## **Form of the Incentive Scheme**

The overall quality of telephone response has levelled up and it would be appropriate to base the incentive scheme on absolute targets for each company. This would have the consequential benefit of eliminating any potential regional bias.

## **Environmental Outputs**

Para 4.71 - The proposal in respect of “amenity issues” and reference to “details of Schedule 9 statement *including* date of last review” is somewhat ambiguous and open ended. This is a matter of concern, given past Ofgem communications in respect of Schedule 9 statements, most notably the Ofgem decision document ( ref 17/03), issued in March 2003. That decision document concluded ( 3.48 ) that “Ofgem does not have a remit to monitor or enforce compliance with Schedule 9 matters”. It would be helpful to understand how Ofgem see how information from the reporting requirement would be used and how this relates to the above Ofgem decision document.

## **General Discretionary Reward**

We suggest that a total annual reward of £1m would provide sufficient improvement incentive. We propose that the discretionary award should be assessed across a range of performance criteria, including:

- Number of complaints per 10,000 customers;
- Number of Guaranteed Standard payments per 10,000 customers;
- Adoption of customer service best practice, in particular to customers on the priority register; and
- Communication with customers, Ofgem, energywatch, media and other bodies during exceptional circumstances.

## **Chapter 5. Distributed generation, innovation funding and registered power zones**

**Views are invited on any of the issues raised in this Chapter and in particular on:**

- **the proposed higher incentive rate for SSE-Hydro based on higher costs;**
- **application of the DG incentive to microgeneration;**
- **reporting arrangements for the DG incentive scheme;**
- **IFI – the criteria that should define an IFI project;**
- **IFI – the practicality and benefit of putting in place interim arrangements for IFI before 1 April 2005;**
- **RPZ – the defining criteria for RPZs;**
- **RPZ – on the practicality of the proposals and the potential barriers that might constrain useful RPZ activity; and**
- **RPZ & IFI – the proposals for an industry-wide good practice guide.**

Para 5.14 Whilst agreeing that the costs of connecting generation should be recovered from generation connections, we remain concerned that the incentive rate will cease should a generator terminate their connection. This is likely to lead us to consider the application of termination charges (to cover non pass through costs) to generators that will need a form of financial guarantee similar to that applied to generation connections by NGT.

Para 5.24 – whilst a 1% O&M cost may be appropriate for EHV connections (which was the subject of the determination referred to in the paper), a higher percentage should be used as an average for all generation connections. An average of 1.5% would be appropriate.

Para 5.38 – The DG incentive regime should apply to all generation types and voltages of connection as it is currently uncertain what patterns of installation will occur and an incentive is needed to facilitate their connection.

Para 5.39 – There appears to be some confusion here between EHV connections and those at HV or LV. With EHV connections made in accordance with the current security standard, generators could expect a continuous connection to the network and hence the proposed regime for network access would work. For connections made to HV or LV networks in accordance with the current security standard, the connections are not planned to be firm and shut downs are part of design of the network to allow routine maintenance to be carried out. Hence for HV and LV connections it would be more appropriate to set a standard of service below which compensation is applicable.

Para 5.41 – any reporting requirements need to be clearly set out before 1<sup>st</sup> April 2005 to ensure that we have appropriate data collection systems in place. Any audit requirements should be undertaken by our external auditors rather than adding further costs with the appointment of another set of external auditors.

Para 5.47 to 5.53 – Whilst agreeing with the objectives of the IFI scheme, it is unlikely to have any significant influence on the level of funding of research but will significantly increase the administrative burden associated with it. To achieve an increased level of funding requires a higher level of pass through. We recognise the need for an open and transparent statement of how projects are selected and managed, however a requirement for a common statement between all distributors is likely to either make this a lowest common denominator document or to significantly delay its completion.

Para 5.54 to 5.59 – Again, whilst agreeing with the objectives of RPZs, there is still a significant administrative burden and risk left with the distributor compared to the level of reward proposed. We recognise the need for an open and transparent statement of how projects are selected and managed, however a requirement for a common statement between all distributors is likely to either make this a lowest common denominator document or to significantly delay its completion.



## **Chapter 6. Assessing costs**

**Views are invited on any issues raised in this chapter in particular on:**

- **DNOs' forecast costs (base case, quality of supply scenario and the DNOs' own scenarios); and**
- **the normalisation adjustments.**

**6.14** Our response to normalisation is covered under paragraph 3.61

### **6.23 Not necessary to adjust DNOs for merger savings**

DNOs can achieve head office and corporate cost savings through being part of a larger group; such savings should be taken into account when comparing DNOs for the purposes of benchmarking

## **Chapter 7. Financial issues**

### **Views are invited in particular on the:**

- **financial ringfence;**

WPD welcomes the introduction of the Special Administration regime and the clarification of the financial ring-fence set out in paragraphs 7.7 to 7.16

### **Treatment of pension costs.**

WPD's reaffirms its agreement with Ofgem's principle that recognition of pension costs associated with regulated distribution and metering activities should be included in the allowed income for DNO's

WPD support Ofgem's view that the liability relating to active members be allocated according to their present employment. As previously stated it is not possible for WPD to classify the activities undertaken by post-privatisation leavers during their entire employment on an individual basis. However, as a pragmatic approximation of their employment history we are able, for South West, to classify individual post-privatisation leavers on the basis of their employment on the date of retirement/leaving. We do not have the data to undertake this classification for South Wales because we do not have historical data, although South Wales total liabilities for South Wales could be allocated based on South West data.

WPD supports Ofgem's approach to allocate pre-privatisation leavers based on the employment costs in the year of privatisation.

WPD would reiterate its view that allocation of pension fund assets should be in proportion to liabilities. An allocation based on a matching assets approach would not, in our view, be practical or possible to achieve with any degree of accuracy.

On the question of over or under provision WPD notes that Ofgem is minded not to make adjustment for over or under funding in relation to past price controls where the pension allowance was not separately identified - hence Ofgem does not proposed to make such an adjustment for the period to 31 March 2005. WPD do not accept that this should be conditional on accepting an unjustified and unfair refusal to fund deficits to the extent that they arise as a result of the use of surplus to fund ERDC's.

In relation to Early Retirement Deficiency Costs, we continue to strongly disagree with Ofgem's view that companies should be penalised for not making payments into the scheme at the time it was in surplus. We reiterate our view that Ofgem should recognise the true benefit to customers from the staffing efficiencies already achieved that result, broadly, to a 70/30 split in favour of the customer. Therefore at least 70% of past ERDC's should be allowed for. It also follows to WPD that penalising those companies that have used surplus wisely in the past for the benefit of customers and their companies would amount to retrospective regulation that incentivises inefficiency..

WPD would support Ofgem with the type of approach outlined which we believe gives Ofgem, customers and DNO's a fair and pragmatic solution.

Finally WPD notes that Ofgem may be thinking of applying a fixed allowance for future service costs. We would strongly oppose this approach as the characteristics of ESPS groups make the approach unreasonable. The level of the future service cost is influenced by factors outside of a DNO's control e.g. the average age of workforce, investment strategy, male/female ratios, mix of pre and post 1988 members etc. Therefore, future service costs should be allowed for in full, as certified by the actuary in the final valuation report for each group. We would be pleased to discuss this point with you further if this would be helpful.

## **Appendix 1. Calculating the capex and opex rolling adjustments**

### **Appendix 2 The losses incentive**

### **Appendix 3 Developing a RIA for metering**

### **Appendix 3 Developing a RIA for metering**

**Risk and unintended consequences.** WPD opposes to the concept that the opportunity to win business out of area is in any way related to the mitigation of the risks of stranded assets and costs..

There is no linkage between the provision of metering services to meet licence conditions in a regulated environment and the provision of metering services in a competitive commercial environment. There is no certainty that any DNO will choose to offer competitive metering services either within or without its licensed area. In practical terms, any income earned from competitive metering cannot compensate for loss of returns on investments made as a regulated business. Those losses must be recoverable through the licensed regulated business.

**Distributional impacts including social impacts** The retention of a capped differential between pre-payment and credit meter services is inconsistent with an objective to introduce competition in metering services.

The whole point of encouraging competition would seem to be to ensure that prices are cost reflective and market related. In the competitive environment there is no possibility of influencing costs to pre-payment customers at the metering services level. Such intervention, if considered necessary, would need to be taken at the electricity supplier tariff level.

### **Appendix 4 Developing a RIA for quality of service**

#### QUESTIONS FOR DEVELOPING THE REGULATORY IMPACT ASSESSMENT COSTS & BENEFITS

##### **QUESTION 1**

What would be the costs and benefits of the proposed changes in each of the areas described above? Can these be quantified?

##### **RESPONSE**

##### **Guaranteed and Overall Standards of Performance**

##### Guaranteed Standard on Supply Restoration

The costs of Ofgem's proposal to separate the supply restoration Guaranteed Standard to cater for normal and severe weather conditions are considered in the section on network resilience.

##### Automatic Payments

We anticipate that in a typical year and during normal weather conditions we would make around 500 payments, total for WPD (South Wales) and WPD (South West), associated

with the 18 hour supply restoration standard. Therefore the total of compensation payments and penalty would amount to approximately £25K.

We estimate that the added costs for field operations and administration would be in the order of £10K.

### **Reviewing the Information & Incentive Project (IIP)**

#### Provision of Disaggregated Interruption Data

We estimate that there would be no additional ongoing cost associated with the provision of disaggregated interruption data by HV circuits and by duration bands.

#### Worst Served Customers

We estimate that there would be no additional ongoing cost associated with the provision of the number of customers experiencing particular frequencies of interruption each year.

#### Form of the Incentive Scheme

We estimate that there would be no additional ongoing cost associated with the retention of the quality of service incentive scheme.

### **Network Resilience**

The net annual cost of the network resilience proposals should limit each companies exposure to 1% of base price control revenue.

### **Incentives for Telephone Response**

We estimate that there would be no additional ongoing cost associated with the incentives for telephone response.

### **QUESTION 2**

What would be the impact of the proposed changes in each of these areas on other incentives in the price control framework (e.g. capex & opex rolling incentives/DG/losses)?

#### **RESPONSE**

We anticipate that the proposed changes in respect of quality of service would have negligible impact on other incentives in the price control framework.

### **QUESTION 3**

Are there any additional costs of the introducing the revised framework to DNOs/Ofgem/other parties? If so, what are these?

#### **RESPONSE**

We do not anticipate that companies will incur any other additional costs associated with the introduction of the revised quality of service framework.

**QUESTION 4**

Are there any impacts on safety?

**RESPONSE**

We anticipate that the proposed changes will have no impact on safety.

**QUESTION 5**

What will be the impact of the proposed changes on the long term reliability of the networks?

**RESPONSE**

We anticipate that the proposed changes will have negligible impact on the long term reliability of the distribution networks (measured in terms of fault rate per kM during normal weather conditions).

**QUESTION 6**

What are the potential costs and benefits of increased investment in network resilience?

**RESPONSE**

One scenario that was considered in the Forecast Business Plan Questionnaire was the impact on network resilience of under-grounding 2% of the overhead line distribution network.

Tables 46 of the Forecast Business Plan Questionnaire submissions for WPD (South Wales) and WPD (South West) indicate the costs associated with the scenario. Tables 48 indicate the anticipated changes in both overall quality of supply and distribution losses for the scenario. Appendices T46-48 of our narrative responses provide background information. We anticipate that under-grounding 2% of the distribution network would result in a minimal improvement in network resilience.

However, our view is that the most cost effective way of improving network resilience is effective operational management which includes ensuring that tree cutting programmes are effective and on schedule. This is consistent with the overall conclusion of the Network Resilience Working Group (NRWG) that the one overriding factor that needs to be addressed in order to improve the storm performance of electricity distribution networks is the proximity of trees to overhead lines.

**QUESTION 7**

What are the potential costs and benefits of increased investment in under-grounding for visual amenity reasons?

**RESPONSE**

Tables 47 of the Forecast Business Plan Questionnaires, for both WPD (South Wales) and WPD (South West) show the costs associated with under-grounding the total distribution networks within Areas of Outstanding Natural Beauty and National Parks.

We anticipate that there would no associated improvement in overall quality of supply or any change in the level of distribution losses.

**DISTRIBUTIONAL EFFECTS****QUESTION 1**

Are these measures likely to benefit all consumers connected to the DNOs' network?

**RESPONSE**

The proposed changes to the quality of service framework are not likely to benefit all customers connected to the distribution network.

**QUESTION 2**

Which consumers are likely to gain most or benefit least from the changes?

**RESPONSE**

The most significant proposed change that would impact directly on individual customers are the incentives associated with network resilience.

The customers most likely to benefit from the proposed changes to the network resilience incentives are rural customers. The customers least likely to benefit are urban customers.

**RISKS AND UNINTENDED CONSEQUENCES**

We have not identified currently any unintended consequences associated with the proposed changes to the quality of service framework.

**COMPETITION**

We anticipate that the proposed changes to the quality of service framework will have no impact on competition.

**REVIEW AND COMPLIANCE**

We do not anticipate we would incur any further costs, above existing and those already identified, associated with the quality of service framework.