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Regulation of Independent Electricity Distribution Network Operators 180/04

Dear Donna

Thank for the opportunity to respond to the above consultation.

We welcome the introduction of Independent Distribution Network Operators. If properly managed and appropriately regulated, these IDNOs could provide more innovative and efficient services to suppliers and their customers.

We would not expect the introduction of IDNOs to result in inefficiencies. For example, neither should the cost to customers rise nor level of service fall merely because they are connected via an IDNO. Where connection is via both IDNO and an incumbent DNO, there should be an obligation on both parties to ensure that this is achieved. The arrangements to meet this obligation, such as the requirement for metering at the interface between the parties, should be left for them to decide. In this case, for example, the decision made should ensure that any lack of metering will not introduce further uncertainty and inaccuracy in the estimation of the Group Correction Factor.

In order to ensure that customers continue to receive an appropriate level of service, all IIP reporting arrangements should apply to IDNOs as they do to DNOs. However the IIP service standards may need to be clarified to reflect that the performance standards of one network may affect another. IIP standards already vary for different DNOs depending on their network characteristics. It should be possible to extrapolate standards for IDNOs using existing models.

The consultation discusses the differences between the charging arrangements for gas and electricity. It suggests that the long-term solution may be to apply similar contractual arrangements as exist in gas to the electricity sector so that one party has direct contractual relationships with each of the other parties. The recent sale of the Distribution Networks has led to this issue being revisited and may result in changes to the gas charging arrangements. It would seem sensible if any long-term change to the arrangements in electricity were consistent with the outcome of these deliberations. We would caution against any solution that increases the complexity or cost of suppliers' systems or creates confusion for customers. A single invoicing system would allow DNOs to develop simple arrangements for the interactions between them.

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We believe that the RPI-X price control regime has worked reasonably well for the monopoly activities of the electricity industry. It has led to considerable efficiency savings to the benefit of customers. As we state above, connection via an IDNO should not result in additional cost to the customer. Therefore the RPI – X approach based on the incumbent DNO's charges with an individual 'X' factor for the IDNO in future years proposed under Option C is the most appropriate if the 'X' factor is capable of being described such that IDNO costs could be tracked after the first year. This approach would allow IDNOs some degree of regulatory certainty.

The financial ring fencing arrangements for incumbent DNOs is necessarily onerous given their size. We agree that they are beyond what is required for smaller IDNOs. While we recognise that the proposals for financial ring fencing are broadly similar to those for IGTs, we believe that an approach based on customer numbers is simplistic. A more appropriate approach would be one based on the revenues at risk should an IDNO face financial difficulties.

If you wish to discuss any of these points, please do not hesitate to contact me.

Yours Sincerely

Terry Ballard
Economic Regulation