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Dear Ms Glass

**Regulation of independent electricity distributors: consultation on implications of licence applications from affiliates of existing licensees**

energywatch welcomes the opportunity to respond to the issues raised by this consultation. This response is non-confidential and we are happy for it to be published on the Ofgem website.

We note the concerns that Ofgem has raised regarding the licensing of an independent distribution network operator (IDNO) affiliated to an existing DNO when compared to the licensing issues which arise in respect of a non-affiliated IDNO.

We agree that there needs to be a balance between ensuring that, on one hand, there is no significant disincentive to market entry for prospective non-affiliated IDNOs, whose presence may increase competitive pressure on existing DNOs to keep connection costs low to users whilst on the other, ensuring that affiliated IDNOs which meet the relevant licensing criteria are not unduly denied the right to operate.

We share Ofgem's concerns that affiliated IDNOs could obtain preferential treatment or hamper competition through the link with an existing DNO. This may occur in a number of ways:

- Where there is lack of transparency of key data made available by existing DNOs to all operators on a non-discriminatory basis, unfairly improving the chances of affiliated IDNOs in obtaining connections work;
- The potential for 'gaming' if low-cost networks are operated by the affiliate IDNO which leaves the existing DNO to operate the high-cost parts of the network. This could then be reflected in higher charges to consumers through its price control; and
- The risk that affiliated IDNOs will be more compliant on levels of service than a non-affiliated IDNO would otherwise be.

We would be keen, like Ofgem, to see the benefits of more competition in connections, as competition ought to bring both more choice and lower costs to users. Therefore, it seems sensible for Ofgem to grant licences to affiliated DNOs to operate within existing DNO areas.

However, in view of the concerns expressed above, we also support the need for sufficient safeguards to appear in the licence of affiliated IDNOs to address these concerns and ensure that adequate protection is provided to all consumers in the relevant distribution area. It should be remembered that affiliates may not have a fully 'arm's length' relationship with their holding company and there may be commercial incentives to behave on the part of either which could create consumer detriment.

We agree that further assessment is needed of whether existing non-discrimination provisions in DNO licences remain 'fit for purpose' or whether additional provision needs to be made to safeguard consumers. There may be some overlap with Ofgem's wider competition law powers. However, consumers should not be left any worse off in terms of their protection under the affiliate IDNO's licence compared to other IDO and existing DNO licensees. Ofgem's suggestion that reporting requirements are firmed up, along the lines of assurance recently agreed by SP Manweb, is worthy of further consideration.

Our concern is that affiliate IDNO licence provisions reflect arrangements on charging which are simple, transparent and consistent with those in other IDNOs' and existing DNOs' licences and which reduce the potential for hidden charging or discriminatory practice. We have no particular preference for any of the suggested price control formulas in Annex 2. However, where there is scope for more innovative and efficient operation by the affiliate IDNO, we would expect those cost savings to be shared with consumers.

Going forward, we will continue to keep these issues under review as and when they are raised, always considering the possible impact on consumers.

We would appreciate being kept informed of the progress of the consultation and any related issues to enable us to comment as necessary.

If you do wish to discuss our response further please do not hesitate to contact me on 0191 2212072.

Yours sincerely

Carole Pitkeathley  
Head of Regulatory Affairs