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Dear Rachel

Delivering the electricity distribution structure of charges project

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ESP Electricity warmly welcomes the decision to implement a common DUoS charging methodology for all DNOs with prices set on this basis coming into effect from April 2010.

In our response dated 14 May to your previous consultation, we supported a common methodology. While we would prefer implementation as soon as practical, and ideally no later than October 2009, we understand why Ofgem considers April 2010 as an appropriate time to introduce the new requirement given the significant shift in direction that this will entail for the DNOs. We also agree that Ofgem should take the decision on the methodology for common adoption and implement it through a collective licence modification.

We agree with the Ofgem suggestion that DNOs should not bring forward further formal modification proposals for the time being. Further we would suggest that other consultations in process—notably those in play from Scottish Power and EDF Energy (for SPN) should be shelved to avoid unnecessary distraction of resources.

Broadly speaking we think the supporting detail on the decision and the project appended to Ofgem's 22 July letter is a firm basis on which to take the project forward. We set out below responses on the specific matters on which you have requested views.

▪ **Whether respondents agree that we should specify the common methodology to be applied across DNOs**

As noted we agree that Ofgem should approve the common methodology and decide between the competing methodologies. Among other benefits a common methodology will create a stable and consistent framework for IDNO investment.

We share Ofgem's belief that the DNOs will not be able to agree a common methodology amongst themselves in a timely fashion. However, there may be merit in allowing them until say the end of December to try to decide on a common basic methodology or at least the key principles on which they are all agreed. This would then leave 15 months until the methodology was to be implemented to establish the detail and backfill the necessary changes. If DNOs should fail to reach a consensus, Ofgem could make the decision instead, by the same date.

▪ **The pros, cons and impacts of each model**

Annex 2 provides a clear statement of relevant principles, their properties and their assessment albeit at a very high level. If there were any doubt, table 1 demonstrates unambiguously why change is needed and illustrates the failure of the ENA-led project in 2005 and 2006 to bring about consistency and cohesion between DNOs.

We do not have detailed views on each of the features that Ofgem has tabulated. We would however make some general points:

- The commentary relates to IDNO charging only once. Any solution should have a common IDNO charging mechanism, and IDNOs should have full input to the form of this part of the preferred methodology. Collaborative work has already begun in anticipation of this;
- Once this IDNO mechanism is set it needs to be allowed to unwind; perhaps there could be a sunset clause that might allow review, but not before 2015;
- There is a key trade off between cost-reflectivity and stability of charges. Stability is very important to IDNOs (and also generators) because of the scale of their investments, especially in an environment where year-on-year changes can fluctuate significantly because of over and under recovery;
- While we have a strong preference for stability and commonality, it is hard to see how the same approach can be adopted for EHV and lower voltage charging given their differing cost characteristics;
- Options that include capping year-on-year changes and giving users the option of a more stable charge based on a prediction of charges into the future would seem to have merit given the government's and the regulator's wider objectives for the sector; and
- Based on the properties we have noted FCP would seem to provide the more stable longer-term charging environment.

▪ **Governance arrangements and the options set out in annex 3**

Notwithstanding our reference above to allowing a bedding-in period for any agreed IDNO mechanism, we feel that an industry code governance arrangement based on the DCUSA model has merit, provided users—including IDNOs—are properly represented. Such an approach with its differentiation between class 1 and class 2 business would allow some items to be progressed without the need for full regulatory scrutiny and would use an existing governance process. It also has merit because of the already established appeals mechanism, though the affordability of this highly legalistic route to smaller players is a moot point.

We doubt the restructuring should be achieved through the separate governance review initiated by Ofgem, and the new arrangement would need to be fast-tracked if the necessary timescales are to be achieved. In this context, we note—and support—the observation in the open letter that DNOs might collectively deliver the project in stages and that they might give priority to IDNO charging ahead of charging at higher voltage levels.

Ofgem is right to identify as an issue the ability of parties other than DNOs to raise change proposals once the common methodology has been implemented. We think this avenue is a prerequisite and strongly disagree that non-DNOs would be likely to bring forward frivolous or uninformed change proposals. They have limited resources to engage in processes of this nature and there would be a self-regulating pressure on them to target resources appropriately.

In this context we would note the emphasis Ofgem is rightly placing on dialogue between DNOs and their customers in DCPR5, and we believe that engagement by IDNOs in the governance arrangements is consistent with this approach.

We agree that price changes should only be implemented at certain times of year (for example April 1st), but see no reason to limit the time when modifications that may lead to price changes could be considered in advance of these dates.

▪ **The proposed processes set out in annex 4**

The timescales and processes look broadly right. The work of the working group should be front loaded where possible to ensure the deadlines are met. Presumably the “common methodology implementation working group” would be a subgroup of the Distribution Charging Methodology

Forum. IDNOs and their representatives should have the right to attendance at all meetings on both the methodology and governance streams.

It would be prudent to change the nature of some of the tasks so that there are defined and immovable reporting points by the DNOs to Ofgem, and any such reports should be made available to stakeholders.

- **Whether there are any other matters we need to consider in light of the decision on a common charging methodology.**

As we have noted in other correspondence with Ofgem, licensing of IDNO affiliates within host areas should be put on hold at least until satisfactory completion of the structure of charges project and a clear non-discriminatory basis established across distribution for charging independent distributors.

Please let us know if you would like to discuss any aspects of this letter further.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'DSpeake', written in a cursive style.

David Speake

ESP Electricity Ltd