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Dear Ms Langford

Gas and Electricity Connections Industry Review 2007-08

Thank you very much for the opportunity to comment on this extremely welcome and important initiative. A transparent, well-understood regulatory policy on connection arrangements is absolutely fundamental to our business, as it will determine the relationship we have with the incumbent distribution network operators (DNOs) and our customers. There is now sufficient a track record to assess how this new part of the market is working and address the various distortions that are apparent.

We have a number of specific points on issues raised within the consultation document and these are addressed in the attachment to this letter.

We also wish to highlight four key issues of principle:

- advantages brought to the distribution sector by IDNOs;
- the need for greater clarity of terms in regulation;
- the need to apply similar principles to policy to both contestable and non-contestable sectors; and
- the need to preclude in-area activity by DNO affiliates until competition stimulated by IDNOs has had time to properly bed in.

The key point we draw from the 2007-08 review is the need to entrench reporting standards. Voluntary measures need to be made compulsory and implemented with penalties that bite for non-performance. Operating in the wider competitive market as we do, we are very familiar with concepts such as performance measures and penalties for non-performance and consequential losses.

In effect the DNOs through the regulatory regime enjoy a special status that shields them from the disciplines of the competitive market. Until proper competition is established on a meaningful scale, we believe their minds need to be concentrated by formal licence requirements and regulated penalties rather than voluntary standards and incentives, which based on passed experience they are able to game.

Advantages of IDNOs

IDNOs bring very significant advantages to the distribution sector. Not only do we provide an important element of competition into a well-established monopoly sector, we also bring disciplines and skills from the commercial construction and services market which benefit consumers. Indirectly we believe we bring benefits to the DNOs themselves by providing a competitive benchmark. However, it is clear we can be seen as a threat by DNOs and our activities are often frustrated by their actions, whether wilfully intended or not.

Consequently this Ofgem initiative represents an important opportunity to review these barriers to our operations and identify measures to remove them.

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Need for greater clarity

Our experience of dealing with DNOs is that these companies will consistently interpret regulation in a way to frustrate our commercial and operating activities. Our typical terms of trade with customers will be based around fixed fees and defined timescales for project delivery. Any failure by DNOs to provide the services we require to time will inevitably have knock-on consequences for our own business, potentially threatening our position in an established relationship and often causing financial harm. It also undermines our reputation in the market. Therefore we believe any service standards should be wide-ranging and explicit in their specification removing any doubt as to their interpretation.

More importantly performance targets need to be set so they are consistent with the most recent standards of performance achieved by the DNOs.

Ofgem has the opportunity with the development of the new price control regime to mandate service standards into the licensing regime as part of its deliberations on standards of service and on setting competitive boundaries. There is abundant evidence from the IDNO community that voluntary measures are interpreted differently by DNOs and simply have not worked.

Disadvantages of affiliates

As a matter of principle ESP Electricity is strongly opposed to the licensing of affiliates of DNOs as IDNOs who are contemplating in-area work. By definition such operations cannot be "independent". The main reasons for our objections are set out in our response to the August consultation on the EDF Energy (IDNO) Ltd consultation.

I hope these views are helpful and would be pleased to provide more detail should you require it.

Yours sincerely

David Speake

Regulatory Compliance Analyst

ESP Electricity

Competition in Connections

October 2008 consultation

Gas Connections

No comments

GT performance against Guaranteed Connection Standards

No comments

Metered electricity connections

The Relative Price Control operating in gas gives IGTs relatively high revenues compared to their underlying operating cost, whereas margins are slimmer for IDNOs?

Margins are slimmer for IDNOs in electricity because of inconsistencies in charging applied by DNOs to the extent that the IDNO can end up paying more in charges to the DNO than would be the case for the DNO charging the consumer on an all-the-way basis. Even if this situation is not in place when a new IDNO network is under development, these circumstances can arise because DNOs rebalance their charges between user types without regard to any consequent impacts on IDNOs. This iniquitous situation, known as margin squeeze, must be addressed as a matter of urgency through the introduction dedicated IDNO charges by the DNOs that specifically lock out the possibility of margin squeeze occurring at any time during the expected operating life of an IDNO network.

IDNO charges must rebalance so the costs we must pay align with the charges we can levy on consumers connecting to our wires. We believe DNO charges to IDNOs need to be set consistently in a non-discriminatory way by DNOs. Our analysis suggests that in many instances a DNO can be better off by an IDNO connecting to its system because it is able to levy more on the IDNO than on the IDNO's consumers themselves were they connected to the DNOs wires. This is surely wrong.

There remain significant barriers to competition in electricity, whether real or perceived, which prevent effective competition from IDNOs and ICPs. If so, we seek consultation responses on the nature of the barriers, and what measures we should consider implementing to address or remove them?

There does appear to be a clear message from the gas industry where there has been healthy development of competition in network asset provision, and where there are formal performance standards and compensation for non-performance. The lesson is that tighter regulation is needed if competition is to be nurtured. Although similar principles have been put in place for electricity, they are not based on formal standards backed up with appropriate sanctions; regulation needs to ensure that the DNOs abide by them.

Metered electricity connections: performance against standards

Why has there been limited reporting against the SLC 15 performance standards, and what measures should be taken to address this issue?

We were very disappointed to read of the patchy reporting against standards by DNOs that is summarised in Table 5:1. Ofgem should as a matter of urgency commission an independent review of the DNOs reporting to ensure they complied with the spirit as well as their interpretation of the letter of the standards.

That said, we believe the real issue is about transparency and timely delivery of estimates and quotations, rather than absolute charges or reporting against standards. Time is of the essence for nearly all new connections, and any delays and complications tend to drive the customer away from seeking competition. We believe it is more important to ensure that we have the simplest, fastest possible approach. All stages of the process need to be transparent with adequate audit trails to ensure that aggregated performance figures can be traced back to each individual component where necessary.

We continue to seek DNO quotations be broken down by hours for the discrete elements of the work, and identify costs relating to materials, labour and plant separately. The information must be available to the DNO for its own costing and internal management purposes, and we can see no reason why it should not be shared with developers. Ideally there would be agreed performance indicators against which the quotations and performance can be measured. Such visibility might also act as a stimulus to some DNOs to improve their own efficiency.

There are standards relating to the provision of non-contestable services where the connection is being provided by an alternative provider. However, the vast majority of contestable activity is still carried out by the incumbent and not all of this activity is covered by service standard reporting. We would welcome feedback on whether it is appropriate to extend the scope of service standard requirements / reporting to the provision of connections not currently covered, and if so, what form the scope extension should take? For instance, we have 30 and 40 day standards for straightforward connections, but no comparable service standards with regard to non-straightforward connections (i.e. the majority of larger connections)

The first objective must be to make the standards work, within the current scope of contestable activity. Making them mandatory for the DNOs through licence conditions would probably help in this process. From ESP's perspective as a developer often considering more complex connections, we believe the standards need to be extended as soon as possible to cover all connections as a matter of urgency.

Data generally suggests that standards are being met. However, this is not consistent with the fact that we receive significant numbers of complaints with regard to service quality from end customers, ICPs and IDNOs. Why is there an apparent inconsistency between reported standards, and the level of complaints received? How should this issue be addressed?

As mentioned above Ofgem needs to commission an independent audit of the data and DNO reporting processes as soon as possible so the data can be validated. Our own experience is that the service we receive from DNOs is not adequate and certainly not of the type we wish to offer our own customers.

Unmetered electricity connections

In the light of this generally disappointing performance, Ofgem seeks views from interested parties on whether they believe that it is appropriate to continue with the current voluntary arrangements, or whether Ofgem should seek to introduce either financial incentives (as part of DPCR5) or specific licence conditions with regard to performance standards in unmetered connections.

The voluntary arrangements should be replaced by mandated arrangements under a licence condition. No financial incentives based on reporting standards should be considered until a thorough independent audit has been carried out on the metered connections data referenced in chapter five. Then they should be considered alongside a matching penalty regime that provides for DNOs to be liable for consequential losses to ICPs and IDNOs in specific circumstances of non-compliance against standards.

Electricity connections: Good practice review

In the light of experience, did Ofgem's Good Practice Review target the appropriate areas?

We believe the review targeted the right areas, but are extremely concerned as outlined above that voluntary reporting standards allow the DNOs too much discretion in judging their own performance. A thorough, comprehensive and independent audit is required as a matter of urgency.

Do the DNOs' reports of their own performance in implementing the Good Practice measures (as per our checklist) accord with their customers' and other market participants' perceptions of their performance? (See Appendix 10 for details of the checklist items, and the traffic light scores for each checklist item.)

See response above.