



COMPETITION IN CONNECTIONS REVIEW 2007/08 DETAILED RESPONSE BY SP ENERGY NETWORKS

1. SP Energy Networks (SPEN) welcomes the opportunity to comment on the issues raised in the paper issued by Ofgem on 16 October 2008.
2. Competition in Electricity Connections is developing rapidly, particularly in relation to networks constructed and retained by or on behalf of Independent Network Operators (IDNOs). The figures in the paper relate to connections carried out, which can lag accepted connection offers by up to 3 years or more. To illustrate the speed at which competition is developing, in the SP Distribution area 58% of estimated connection acceptances in 2007/08 weighted by final supply points were accounted for by non-affiliated ICPs or IDNOs. IDNOs accounted for 31% of the market on this measure.
3. It seems clear that in the gas connections market IGTs are steadily growing market share as a result of subsidised connections through adoption payments, which average some £300 per connection. GDNs are disincentivised from making such payments due to their regulatory treatment by Ofgem for price control purposes (i.e. they are excluded from the RAV). IGTs now account for more than half of all gas connections, and for nearly all adopted connections. We think that it is right to consider whether the approach to adoption payments and relative price control remains appropriate in gas. The same question should be asked in relation to electricity connections in view of the rapid growth of IDNO networks in particular DNO areas. At the same time we also question the need for a continuation of highly detailed standards of performance for gas connections on “Better Regulation” grounds.
4. We are disappointed that the paper focuses on differences in competitive market shares between the gas and electricity connections markets, without more analysis of the underlying differences between the two, including:
 - In the case of gas, a broadly homogeneous technical and operating environment across GB, with few if any regional variations in working practices and network configuration;
 - In gas, provision for guaranteed capacity for schemes within a standard matrix of load and pipe sizes;
 - In gas, a self-connect regime for schemes within pre-set parameters by accredited service providers;
 - In the case of electricity the need for boundary equipment between networks which serves a number of purposes, including protection of customers on one side of the boundary from faults on the other side.

5. In addition, we are puzzled at the lack of analysis of differences in measures of competition between DNO areas. We would have expected more of a distinction to be made between DNO areas where virtually no competition appears to be taking place from those where competition is well established and developing. In addition, the inclusion of service alterations in the total number of connections is inappropriate, as these tend to be smaller, one-off jobs that do not attract interest from non-DNO connections providers.
6. In view of the extent to which effective competition has now developed in the two SP licensed areas, we believe that it is now appropriate for consideration to be given to treating connections as fully excluded services for SPD and SPM.
7. Our detailed comments on the questions in the paper are set out below.

Chapter two: Question one: *Is the data we have collected reasonably representative of connection charges levied by GDNs and IGTs, and adoption payments made by IGTs and GDNs?*

8. One difficulty in interpreting the data is the absence of figures for charges by ICPs. It is also not clear how the figures in gas are affected by the prescribed allowances in relation to domestic connections (the 10m/23m rules). Paragraph 2.11 says that average IGT charges amount to £200 per connection. We assume that this is gross of adoption payments paid to ICPs, as it is otherwise difficult to reconcile this average figure with the graph on page 13 (figure 2.2).

Question two: *Are adoption payments the main reason why ICPs have a much higher market share in connection to IGT networks than GDN networks? Are there other factors that account for the fact that only 5% of connections to GDN networks are installed by ICPs?*

9. It seems likely that adoption payments are the main factor involved.

Question three: *What factors enable IGTs to make adoption payments of these magnitudes? Do they have lower costs of operation, or are other factors at play, such as the degree of headroom in the relative price control?*

10. It seems likely that a number of factors are relevant here, including relatively low operating costs for new networks constructed by IGTs. We believe that for both IGTs and IDNOs the headroom available in relative price control and the provision of adoption payments tends to skew the market for connections in their favour.



Question four: *What factors lead IGTs to charge lower connection charges? Are ICPs/IGTs more efficient at installing the connection or are other factors at play?*

11. It seems likely that the average figure for GDNs is affected by proportionally more large connections.

Question five: *What impact does the contrasting nature of GDN and IGT price controls have on competition in gas connections*

12. See response to question 3.

Chapter three: Question one: *We seek consultation response on whether stakeholders agree that performance standards are as high as reported, and what lessons can be learnt from the gas connections industry and applied to the electricity connections industry.*

13. As set out above, we think that there are some features of the gas connections market that make it easier for independent connections providers to operate than in electricity. These include the self-connection provisions and the more homogeneous technical environment. However, these features are not readily applicable in electricity distribution due to historical and other factors.
14. As an example of the technical diversity in electricity distribution, there are over xx types of LV cable jointing systems currently in use. As any jointing problems with cable may take years to come to light, and involve significant costs on the part of the distributor, the latter needs to be satisfied as to the system used by an independent connections provider and the workmanship of the individual jointer.
15. As regards self-connection, SPEN already operates a live-working regime at LV which accredited ICPs and authorised jointers can participate in. Selection of a Point of Connection (POC) would be more difficult in electricity due to factors such as voltage drop.
16. In relation to reported figures under performance standards, it needs to be borne in mind that these may be less meaningful (but also less burdensome) in DNO areas where third party connections are relatively few. Achieving 90% performance for provision of 50 POC quotations within stated timescales involves fewer resources than provision of 90% of 500 such quotations.
17. We are also puzzled why the paper does not question the continued need for highly detailed performance standards in gas connections.

Chapter four: Question one: *Why has competition been slow to develop in electricity connections compared to gas, and what measures if any, should be taken to address*

this issue. In particular, we seek responses on the following theories for the relatively slow growth of competition in electricity connections:

a. The relative price control operating in gas gives IGTs a relatively high revenue compared to their underlying operating cost, whereas margins are slimmer for IDNOs?

b. 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 should be implemented to address them?

18. As set out above, we think that there are a number of factors that have favoured competition in the gas connections market that are not mentioned in the paper, including
 - The charging and connections regime for GDNs facilitates the provision of a ‘self-connect’ regime with guaranteed pressure and capacity within given parameters;
 - A homogeneous technical and operating environment across GB has assisted players in the competitive market.
19. The paper does not sufficiently recognize the speed at which competition is becoming established in electricity, particularly in relation to IDNO and DNO out of area networks. The figures that are set out reflect schemes that were planned and accepted up to 3 or more years previously. More up to date figures indicate that IDNOs in particular are rapidly expanding their share of the connections market. In SP Distribution’s area, its share of connection quotation acceptances (including affiliates) measured by end-users was only 42% in 2007/08, with IDNOs accounting for 31%.
20. It should also be noted that overall measures of competition may be distorted where service alterations are included in the base, as these tend to be lower value one-off jobs that do not attract competitive interest. We would also expect analysis to take account of competition by size category of schemes (e.g. number of plots or kVa).
21. We believe that the ‘headroom’ in IDNO price control and the provision of adoption payments tends to skew the connections market in favour of IDNOs .

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

22. We do not see this as an issue distinct from that of the extent to which third parties are seeking competitive connections and provision of non-contestable services in particular categories.

Question two:

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. Therefore we seek 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).

23. There are reporting requirements in relation to provision of LV connections within 30 or 40 working days, but these are not ‘standards’. We do not see a case for introducing standards covering larger connections, as these tend to involve a diverse range of circumstances, including variations in the complexity and timescales of wayleaves/consents. For example, in some cases Section 37 consents may not be given for some years. In addition, a number of DNOs put out to tender construction works for larger schemes, and these take time to process. For larger schemes, procurement of equipment such as transformers or switchgear is also a factor influencing the time period for delivery of a project.
24. Where a customer is concerned about the time taken to provide a connection service, we ask them to come to us and discuss the matter to see what can be done. Connections-related communications with customers will normally include a contact point for any queries, and contact points are also set out on our website (spenergynetworks.com). There is a clear escalation process if the customer wishes to take the matter further. Certain matters are of course within Ofgem’s enforcement or determination remit.
25. As mentioned above, we think that the need for such detailed performance standards in gas connections should be reviewed, rather than considered as a possible model to be applied in electricity.

Question three: *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?*

26. We are not aware of significant numbers of complaints from customers when set against the high volume of connections and non-contestable services quoted for and provided each year in SP’s operating areas. The paper does not provide figures for these complaints or further details of the issues involved.



Unmetered Supplies

Chapter Six: Question one: *In the light of 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.*

27. It is important as a first step that reporting is on a consistent basis. It is evident, for example, that some DNOs are reporting on a 'per lamp' basis and others on a 'per job' basis in some categories.
28. SP considers that the figures reported to Ofgem tend to understate its underlying performance due to delays in internal processing of completion reports. In our opinion this is borne out in dialogue with local authorities who appear generally satisfied with the level of service provided.

Chapter seven: Question one: *In the light of experience, did Ofgem's Good Practice Review target the appropriate areas?*

29. We think that the appropriate areas were targeted.

Question two: *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.)*

No comment.