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	159/08	0117 933 2175	10 February 2009

Dear Rachel

**Ofgem Consultation: Electricity Distribution Price Control Review Policy Paper
December 5th 2008**

This response is provided on behalf of Western Power Distribution (South West) plc and Western Power Distribution (South Wales) plc. In addition to this letter we attach an annex of answers to the specific questions raised in your policy paper, together with a further appendix focusing on a number of detailed customer-related issues.

We are also submitting our detailed business plan for 2010-2015. It should be noted that in preparing the plan we have made some assumptions about policy issues that have yet to be resolved and these are attached to this letter cross-referenced to the appropriate section of our response.

WPD supports the three key objectives that Ofgem identified in their initial policy document and the effort being made to assess outputs in these three key areas for stakeholders. It is clear from the RORE calculations that there is a wide range of returns achieved by individual companies and this assessment should be compared to performance against each of the objectives when assessing DPCR4 performance and this can also provide a basis for target setting in DPCR5.

Environment

It is important when assessing a DNOs environmental performance that there is a consideration of three areas:

- Research to plan for the future
- The internal actions a company takes to reduce its carbon footprint
- Innovative actions taken during the course of DPCR4 to facilitate a low carbon future

Clearly DNOs should demonstrate that these areas are underpinned by specific, clear and measurable goals in order that Ofgem can measure relative performance.

Ofgem quite correctly emphasises that it wishes to encourage innovation but innovation implies action either taken or committed. Areas such as use of system charges and IDNO connection charges are clear areas of failure to deliver for some DNOs.

Ofgem could make appropriate comparisons in the following areas:

- Structure of Charges
- ISO 14001 Environmental Management Standard
- Fluid filled cable leakage and SF6 loss
- Environmental incidents and prosecutions

Customers

As a DNO that has totally changed its approach to customers over the last 15 years we believe we are uniquely positioned to comment on the assessment of DNOs in terms of customer service. WPD 15 years ago held the dubious honour of holding 13th and 14th position in nearly every aspect of customer service and reliability when compared to other DNOs.

The change came about by focussing the whole company on the importance of treating all customers including communities, generators, IDNOs, suppliers as well as domestic industrial and commercial customers in the way we personally would wish to be treated.

These aspects were underpinned by specific, clear and measurable goals and much of that information is available to Ofgem in terms of comparing DNOs:

- Complaints and determinations
- CML and CI performance
- Call centre performance
- Guaranteed Standard failures

Networks

Ofgem has a wealth of information in terms of system performance through IIS. It also has the normalisation of network performance in order to determine the severity of targets. However with the exception of long run CI performance it has not got an effective measure of network health.

In some cases network investment proposals for DPCR4 were in our view exaggerated and even when Ofgem cut those forecasts some companies have failed to deliver with various explanations:

- Technological breakthrough has removed the need to spend capital
- Resource constrained capex
- Capex deferral
- Capex efficiency

Technological breakthrough is possible but development in the electricity sector is generally slow and well signposted over many years.

We believe that companies should have been aware going in to DPCR4 that it is a normal part of any business to replenish an aging workforce and have a resource plan prior to this review period. There is a history over many years of a lack of recruitment, training and role development across DNOs.

Capex deferral should not be rewarded when in retrospect it is established that it was not required in the business plan.

We believe that in the absence of health indices there are few areas that Ofgem is able to assess in terms of the efficiency of network investment.

The suggested comparisons between companies should cover the following areas:

- Forecasting and reporting accuracy
- Investment against forecast
- Efficient delivery
- Resource planning

We look forward to further constructive discussions with you and your colleagues in order to resolve the outstanding policy issues between now and June and develop our suggestions for performance comparisons.

Yours sincerely

A handwritten signature in black ink, appearing to read 'AS', with a stylized flourish extending from the bottom right.

ALISON SLEIGHTHOLM
Regulatory & Government Affairs Manager

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Attachment

Business Plan Policy Assumptions

In conjunction with this response, in order to submit a plan that accurately reflects our future expenditure we have made a number of assumptions, listed below:

Component	DPCR4 treatment	Ofgem DPCR5 initial views	WPD view	WPD response reference
Controllable opex	Part-capitalised – this element subject to capex incentive, rest ex ante only	Totex approach – sharing factor (paragraphs 4.60 - 4.62)	Equalisation of opex/capex incentive	Page 20 Question 5
ESQCR/TMA costs	Specific re-opener	Totex approach –sharing factor (4.60 - 4.62)	Efficient expenditure included in FBPQ	FBPQ
Non-controllable opex (business rates, Ofgem licence fee)	Pass through	Pass through	Pass through	
Pension valuation		Three Options (5.41) Option 1 – use latest triennial valuation with DPCR6 true up Option 2 – use DNO best assessment for DPCR5 Option 3 – re-opener during DPCR5 for material valuations from triennial valuation	Option 3	Page 24 Question 2
Network investment	Subject to capex incentive	Totex approach –sharing factor (4.60 - 4.62)	Fixed portion of costs into RAV	Page 23 Question 9
Materials costs	No index	Considering index (4.49 - 4.55)	No index. Ex ante approach with trigger mechanism	Page 19 Question 4

Component	DPCR4 treatment	Ofgem DPCR5 initial views	WPD view	WPD response reference
Customer numbers	Revenue volume driver	Possible conx capex driver (new customers only) (4.44 - 4.48)	Remove customer numbers from price control formula Variable allowance for capex above baseline	Page19 Question 3
Units distributed	Revenue volume driver	Capex driver for general reinforcement – only where increased demand requires it. (4.44 - 4.48)	Remove units distributed from price control formula Variable allowance for capex above baseline	Page 19 Question 3
Corporation tax costs	Ex-ante assessment	Possible sharing factors for legislative changes (5.23 - 5.24)	Cap/collar for legislative changes	
Financing costs	Ex-ante assessment	Possible triggers for cost of debt (5.9 - 5.13)	Triggers not supported	Page 24 Question 1
Return on Regulatory Measure (RORE)	None	RORE measure to assess DNOs' performance against the overall price control package	RORE measure	Page 3 Question 4
IQI forecasting accuracy	IQI forecasting accuracy	Constrain changes to DNOs detailed business plan submission	Retain with an RORE incentive on accuracy	Page 1 Question 2 Page 20 Question 6
Capex rolling Incentive	Companies bear a portion of capex overspend	Output measures incorporated into a RORE mechanism	Output measures incorporated into a RORE mechanism	Page 20 Question 6
Losses	Output measure	Output measure – based on common reporting requirements. Tougher targets for DNOs investing in low loss equipment as part of FBPQ.	Input measure for technical losses. If output measure adopted should be cap and collar at 50% of IIS RORE.	Page 8 Question 7
Business Carbon Footprint (BCF)	None	League table based on reporting against GHG protocol	Exclude contractor performance from reporting	Page 8 Question 8

Component	DPCR4 treatment	Ofgem DPCR5 initial views	WPD view	WPD response reference
SF6	None	No separate incentive needed. Include within BCF	Include within BCF	Page 8 Question 8
Fluid-filled cables	None	None. DNOs to subscribe to Operating Code and report incidents to Ofgem/EA. And use IFI for R&D leak detection technology	None Subscribe to Operating Code	Page 9 Question 10
Connections	No margin allowed on competitive connections activities	Allowed regulated margin on competitive connections activities for all DNOs	WPD do not support the introduction of a margin on connections activities.	Page 13 Question 4
DG incentive	Ex-ante assessment	Ex-ante assessment	Ex-ante assessment with embedded generation treated as relevant DG	Page 7 Question 4
Transmission grid exit charges	No incentive	Possible Incentive	No incentive	Page 7 Question 6
Demand and generation revenues	Separate revenue caps	Separate revenue caps until revised cost reflective charging implemented	Single pot for demand & generation	Page 7 Question 4
RPZ	Up to March 2012	Up to March 2012, then within new Innovation Incentive		
IFI	80% pass through subject to overall cap.	80% pass through subject to overall cap	80% pass through subject to overall cap.	
Innovation incentive		Possible incentive Option 1 – ex-ante, 100% funded Option 2 – individual project assessment during DPCR5, partial up front funding with reward based on project outcome. Possible fund administered by Ofgem Option 3 – ex-post project outcomes assessed by end of DPCR5 – with rewards/penalties applied	Option 2. Assessment of individual projects.	Page 7 Question 5

Component	DPCR4 treatment	Ofgem DPCR5 initial views	WPD view	WPD response reference
Transmission exit charges	Pass through	<p>Option 1 – ex-ante assessment with re-opener</p> <p>Option 2 – capacity volume driver plus mechanism to identify avoided or deferred reinforcement</p> <p>Option 3 – partial pass through combined with options 1 or 2.</p>	Pass through	Page 7 Question 6
Worst-served customers	None.	Defined allowance with an average cost per customer cap – “use it or lose it”	Defined allowance in FBPQ based on DNO costs supported stakeholder engagement.	Page 15 Question 7
AONB	Ex post assessment Cap per km of cable by voltage level	<p>Ex post assessment</p> <p>Option 1 – continue with voltage caps per km of cable</p> <p>Option 2 – overall cap per km of cable</p>	Overall cap sufficient to fund “iconic schemes” identified by stakeholders	Page 9 Question 9
IIS	Output measure 3% of base revenue exposure = +/- 1.6% allowed return on equity	<p>Output measure</p> <p>Should the level of risk/reward be increased?</p> <p>Should there be a 10 year incentive?</p>	Output measure - continue with 3% of base revenue over 5 years.	Page 13 Question 5
Customer service	Ex-post assessment	Ex-post assessment with mandatory adoption of best practice in scheme or licence	Ex-post assessment with voluntary adoption of best practice	Page 17 Question 8