

Hannah Nixon
Director, Regulatory Review
Ofgem
9 Millbank
London SW1P 3GE

Central Networks East plc
Pegasus Business Park
Castle Donington
Derbyshire
DE74 2TU
central-networks.co.uk

Jonathan Ashcroft
T 02476 185766
Jonathan.ashcroft@central-networks.co.uk

Thursday 23 April 2009

Regulating energy networks for the future: RPI-X@20 Principles, Process and Issues

Dear Hannah

I am pleased to provide the views of Central Networks in respect of the first consultation paper in this very important review.

RPI-X has been very successful in yielding significant benefits to customers with price reductions of some 60% since privatisation and providing incentives for companies to drive these efficiency improvements.

However, the original framework was of necessity focused on cost, and has since had to adapt in successive price controls to keep pace with the additional drivers on Distribution Network Operators (DNOs) which result in increased roles or costs. For example, Distribution Price Control Review (DPCR) 3 was enhanced by the incorporation of the quality incentive, providing additional rewards (or penalties) for improvements (or deterioration) in network and telephone performance. DPCR4 was further enhanced to fund increased Research and Development and incentivise efficient connection of Distributed Generation.

New Challenges

Given the new and uncertain challenges now facing the energy industry, and more specifically DNOs, we fully support Ofgem's review ahead of the framework's 20th anniversary.

The consultation rightly points to the huge uncertainties brought about by the 2020 targets, including aspirations around transport and buildings, whilst



Central Networks East plc
2366923

Central Networks West plc
3600574

Central Networks Services Limited
Registered Office:
Westwood Way
Westwood Business Park
Coventry CV4 8LG

maintaining security of supply. The implications of these are highlighted within the LENS report in terms of the possible nature of future energy policy and hence technologies, how people will use energy, and the timescales for change and scale of adoption. The impact on distribution networks, and hence the roles DNOs undertake and behaviours we will need to display, are uncertain. They will, however, require us to continue to improve the relationships we have with key stakeholders and customers as well as taking a more proactive role in facilitating future energy markets, potentially requiring more speculative investment ahead of need.

Given this vision, whilst we would on the whole concur with the objectives for the review outlined in the consultation, we believe they could be extended as follows:

- Enable a future low carbon energy market through leadership and delivery of a secure and sustainable network;
- Invest appropriately in order to provide those secure and sustainable networks;
- Strive for increasing efficiency, innovation and appropriate quality of service; and
- Engage in and respond to the needs of current and future consumers and society.

Direction for change

RPI-X has provided significant benefits for customers, incentivising DNOs to minimise costs through focusing on our core competencies. Where we would therefore disagree with the "consensus view of today's energy network companies" presented in the document is that DNOs are in themselves:

- Low risk and potentially risk averse;
- Willing to undertake investment only when commitment is provided by users/regulator;
- More focused on Ofgem rather than understanding our own customers' needs;
- Reactive to developments in government policy rather than proactive;
- Reluctance to innovate; focused on their own businesses but not interactions with markets.

This unfortunately one-sided caricature fails to give due credit for constructive actions that we have taken and are taking today to understand our customers and stakeholders needs, and develop innovative solutions to their problems.

Where these behaviours do exist, they stem from either the cost focus RPI-X has

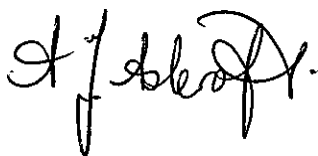
driven in networks or directly from the incentives within the current regulatory framework. In this respect they do provide a list of issues to be addressed by the review of RPI-X, and are directly related to the new challenges we have highlighted above.

Key therefore to the whole debate is the potential increased role networks are expected to take in facilitating future energy policy and consumer requirements. In determining this role, who is the guiding mind? To what extent will this dictate costs or investment ahead of any firm commitments? And who therefore ultimately bears those associated costs and risks? Each of these questions is rightly captured within the consultation and should form the primary deliverables of the review.

As highlighted at the start of this response, we see this as a significant project in shaping the future role of networks and hence are keen to support it. I have therefore put forward myself and Jeff Douglas for the future working groups via the ENA and I am eager to build upon the level of involvement achieved to date.

I look forward to progressing these issues through the working groups and beyond but I can be of further help in the interim please don't hesitate to contact me.

Yours sincerely



Jonathan Ashcroft
Regulation and Commercial Manager