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DPCR5 Response
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Dear Sirs

**OFGEM Consultation Ref. 128/09
Electricity Distribution Price Control Review Initial Licence Drafting**

I am responding to this consultation document with comment relating specifically to the Connections section. The letter can be treated as non-confidential.

Davis Langdon provides cost consultancy services to the commercial market place across the UK and energy consultancy services across the whole energy spectrum. We maintain a wide portfolio of energy connection schemes but generally operate with developers seeking relatively large connection demand or generation capacities.

Over time we have facilitated many schemes that have either been constructed by independent connection providers and adopted by the incumbent DNO (and more recently by IDNOs) or constructed by the DNO connection business.

The consultation seeks answers to four specific questions which I will address on a general basis. The development of a competitive connections market has been very slow as shown by the annual Connection Industry Review. The planned timetable for the DPCR5 period requires DNO to implement new reporting procedures and install systems and processes for the purposes of compliance with the Electricity (Connection Standards of Performance Regulations) 2010 (SI 2010/1234) and any Connection RIGs issued by the Authority under standard condition 15A (Connection policy and connection performance) but could see DNOs, legitimately or otherwise, deferring for as long as possible before verifying systems and processes.

The SI, the Regulations and new Licence Conditions (15A and CRC13) are mandatory whereas in the past licensees have been left to voluntarily adopt any competition in connection initiatives; and they have failed woefully. We fully support these proposals albeit with some reservation on allowing the DNO to charge a regulated margin followed by an unregulated margin by December 2013. I will explain the reason for this.

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Davis Langdon has for some years edited a number of Spon's price books which are generally accepted as an industry standard. Two of these relate specifically to Mechanical & Electrical Services and Civil Engineering & Highway Works. We encounter far too frequently, connection offers from DNOs for contestable and / or non-contestable work where there is no cost breakdowns provided and if they subsequently are, they hold very little correlation to any of the activities the DNO are expected to perform. The DNO claim that any divulgence of cost information is commercially sensitive but fail to elaborate the reason why. The services we provide our clients also extend to quantity surveying so we are well informed when assessing planned costs and out turn costs. We generally find that DNO non-transparent pricing results in a significantly higher cost than our cost projection and in some cases for highway works, 3 or 4 times higher. It proves impossible to obtain an accurate breakdown of a DNO quotation to assess how any scope of work is priced, what level of overheads and prelims are applied and more importantly whether the quotation is cost reflective.

We know that DNOs are not allowed to make a margin on connection work and introduction of a regulated margin arguably levels the playing field for the DNO against ICPs. However, there remains a suspicion that the lack of transparency is hiding a margin or a cost recovery not wholly attributable to delivering the connection. We also accept the argument that a lack of competition in some DNO areas may be down to the fact that there is no profit to be made on connection activities. Allowing a 4% regulated margin could stimulate a market. Where there is a lack of transparency the DNO is able to smear costs across non-contestable work and make the contestable work package look attractive when compared to an ICP. Allowing a 4% regulated margin would not then stimulate the market.

The framework proposed under DPCR5 is able to provide the stimulus needed as long as the Regulatory and Industry Guidance require the DNO to present their costs in a transparent and commercial way. DNOs claim not to be commercial organisations to justify their behaviour and introducing a commercial mechanism to incentivise their performance requires them to behave differently.

The CRC13 proposal provides a mechanism for the licensee to issue a Regulated Margin Notice providing the systems and procedures are verified. The proposal also allows the Authority to issue the Connection RIG that could mandate a DNO to deliver transparency. Currently the level of detail provided is voluntary and has been woefully ineffective.

The SI / RIG / LC proposal seem to be self regulating in that a DNO not aspiring to charge a regulated margin may have something to hide. There does not appear to be any time constraint on DNOs but it maybe that compliance to CRC is similar to standard licence conditions in that compliance is absolute. We think that this should be made clearer otherwise DNO could delay until nearer December 2013. Why comply to earn 4% when the existing cost recovery exceeds the cost?

The consultation also discusses a price accuracy scheme which is aimed at the segmented markets where no competition is expected. While this is still under discussion, the requirement for accurate pricing should consider extending to licensees in segmented markets where competition is expected and where the licensee has failed to issue a Regulated Margin Notice. The conditions require a licensee to apply the regulated margin across all segments but if they choose not to, should be subject to some other mechanism to protect customers.

Ultimately the failure to meet competition test by December 2013 poses a risk to the licensee of a Competition Commission referral. We would like to see competition developing at a faster pace post April 2010 with December 2013 as the back stop date for DNO meeting the competition tests. If compliance with CRC13 is not absolute, theoretically DNOs could continue at present without a regulated margin until say, October 2013, verify systems and meet competition test in a single process and apply unregulated margin without a transparent transition. We harbour a mild concern that DPCR6 could have opened up by December 2013 and DNOs use this to deflect any threat of a referral. We would like to see the Connection Industry Review (as well as compliance with CRC13) to continue to act as a barometer and for the Authority to review annually the competition tests where competition is failing to develop.

We will continue to monitor developments in the industry and look forward to the final proposals expected later this year as well as the further consultations early in 2010 for implementation on April 1st 2010.

Yours faithfully

David Clare
Consultant