



## Interested Parties

*Promoting choice and value for  
all gas and electricity customers*

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Date: 1 July 2011

Dear Interested Party,

### **Publication of Electricity North West's Competition Notice.**

#### Background

In Distribution Price Control Review 5 (DPCR5) we introduced a new approach to facilitating competition in connections to electricity distribution networks<sup>1</sup>. Since 1 October 2010 DNOs have been allowed to earn a regulated margin (4 per cent) above cost<sup>2</sup> on connection charges in certain Relevant Market Segments<sup>3</sup> where competition is considered viable. The purpose of the headroom created by this regulated margin is to attract new market entrants and ultimately benefit connections customers through the pressure that new market entry brings to raise efficiency, lower prices and improve service.

In addition to this regulated margin, in our DPCR5 proposals we also made provision for DNOs to submit a Competition Notice to charge an unregulated margin in the Relevant Market Segments. This opportunity to earn an unregulated margin was designed to encourage a change of mindset by DNOs with regard to competition and stimulate the removal of potential barriers to competition. To further encourage DNOs to actively think about how they can facilitate competition we also set out that any DNO that failed to demonstrate competition, or put forward a case by December 2013, would be reviewed by Ofgem and could subsequently be referred to the Competition Commission.

These developments were inserted into the Electricity Distribution Licences of the various DNOs as Charge Restriction Condition 12 (CRC 12).

#### Electricity North West's (ENW's) Competition Notice

On 6 June 2011, in accordance with the requirements of CRC 12, Electricity North West (ENW) submitted a Competition Notice to Ofgem. This Competition Notice serves as an application by ENW to charge an unregulated margin on contestable works in all of the Relevant Market Segments set out in CRC 12.

<sup>1</sup> Please refer to DPCR5 Final Proposals - Incentives and Obligations for further information <http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=348&refer=Networks/ElecDist/PriceCtrls/DPCR5>. The detail of the obligations on DNOs are set out in CRC 12 of their licences.

<sup>2</sup> Previously under DNO approved connection charging methodologies their connection charge were limited to recovery of reasonable costs.

<sup>3</sup> Relevant Market Segments as defined in CRC 12

The ability to charge an unregulated margin (constrained by competition) will be allowed where DNOs demonstrate that they have passed both a Legal Requirements Test and a Competition Test, both set out in CRC 12 and the DPCR5 Final Proposals document<sup>4</sup>.

Essentially, the Competition Test is designed to enable DNOs to demonstrate that the market for electricity connections in each Relevant Market Segment is working effectively for customers.

The process for assessing a Competition Notice submitted by a DNO is set out in CRC 12 and the DPCR5 Final Proposals document. Following receipt of a Competition Notice we will consult with parties that we believe have an interest in the Notice before determining whether the Legal Requirements and the Competition test have been satisfied. Ultimately, in assessing a Competition Notice we will be looking at whether we can rely on real competition or the threat of competition to protect consumer interests rather than regulation of the margin earned by the DNO.

We are in the process of preparing a consultation document on the ENW Competition Notice which we intend to publish in mid July. This document will set out our initial assessment of ENW's application and highlight particular issues on which we would welcome respondents' views and evidence. In the meantime, we are (with ENW's consent) today publishing a copy of ENW's Competition Notice on our website (as an associated document to this letter). This because of the impending summer holidays and is intended to allow interested parties the opportunity to consider ENW's application ahead of the formal consultation.

Interested parties should make their comments known to us through the formal consultation process in due course. However, if you have any questions about this letter or any other aspects of the Competition Test process please contact Rebecca Langford (contact details above) to discuss.

Regards

A handwritten signature in blue ink, appearing to read 'Rachel Fletcher', with a stylized flourish at the end.

Rachel Fletcher  
Partner Local Grids

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<sup>4</sup> <http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=348&refer=Networks/ElecDist/PriceCntrls/DPCR5>