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**Consultation on regulatory measures to address the effects of gross volume correction and other settlements data adjustments on the distribution losses incentives mechanism.**

Dear Lesley

E.ON welcomes the opportunity to this consultation and the proposed solutions.

We have provided answers to the specific questions raised within the consultation, but we also have concerns regarding the consultation, both in inaccurate statements that are made within it and the legitimacy of the methodologies being proposed. We will deal with these points separately.

#### **CHAPTER: One**

Paragraph 1.1 of the consultation states the following

"1.1. Ofgem introduced a losses incentive mechanism in the third electricity distribution price control (DPCR3) to provide a financial incentive (reward or penalty) to encourage the DNOs to manage the level of losses on their networks. Losses can be reduced by making appropriate investments on distribution networks, optimising network operation, influencing users, working with third parties to improve the quality of data and reducing theft."

We believe this statement is very important as it gives a view of what DNOs can be expected to do to reduce losses

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other than technical losses. It is our view that some of these activities could result in adjustments to data that we have seen.

## **CHAPTER: Two**

Paragraph of the consultation reads as follows;

"2.16. The Authority agreed that the reported losses for these DNOs in 2009-10 were abnormally high as a result of unconventional settlement data adjustments, were unrelated to network performance, were outside of DNO control and would not have arisen if these adjustments had not occurred. The Authority therefore felt it was appropriate to grant these DNOs relief from the application of the penalty rate of interest and the effect of over-recovery on future tariffs."

It is our opinion that this statement is not wholly accurate. Our analysis shows that some of the data adjustments carried over this period were within the control of the DNO. We have many sites where adjustments have been made due to receipt of late or incomplete data from DNOs. We therefore believe that this does sit within the wider remit of the losses incentive.

Paragraph 2.28 reads as follows

"2.28. The industry set up a Distribution Charging Methodologies Forum (DCMF) Working Group (comprising representatives from DNOs, suppliers, Elexon and Ofgem) in response to concerns regarding the adjustments to data and the resulting impact on charges. The group has considered the settlement data issues which have given rise to the problem, and has discussed the different methodologies put forward. Following group discussions, several modifications to the BSC are being proposed, in order to improve settlements data accuracy going forwards."

The unanimous conclusion from this working group was that the Losses incentive mechanism was not fit for purpose and the group wrote to Ofgem to state this. The DNOs on the group took it on themselves to raise modifications to BSC that would mitigate the effect of GVC on the inadequate losses incentive. These modifications are not intended to improve settlements data accuracy and do not do this. At the Ofgem workshop in December one of the DNOs in their presentation to the group stated that the work Suppliers had carried out had improved the accuracy of data. The BSC modifications are based on the belief that GVC corrections may be anti competitive not on the premise that GVC corrections make settlement data less accurate.

**Question 1:** Do you think we have identified the main data/billing adjustment techniques used by electricity suppliers and their impacts?

Suppliers use many techniques to improve data within the industry and to increase settlement performance. Over the period in question E.ON and the Suppliers industry average Settlement performance has shown steady improvement partly driven by adjustments to data. Reducing the ability to make adjustments such as GVC is in conflict with the earlier statement as to the purpose of the losses incentive. The modification to the BSC that seeks to stop GVC altogether therefore should be rejected on these grounds by Ofgem as it does not improve the quality of data but reduces it.

**Question 2:** Are there any other factors you think we should take into consideration in assessing the impact of settlement data volatility?

We believe that Ofgem need to look at the number of adjustments that have been made to correct data inaccuracies caused by the DNOs themselves. For example we are still awaiting 1792 D0171 flows confirming sites have been disconnected from 2010. This is despite considerable effort on our part to chase these missing flows. We hope to be in a position to provide further supporting evidence to Ofgem where the DNOs are directly responsible for the inaccurate data in settlement. Where this is the case we believe that DNOs should bear the consequences as is the spirit of the losses incentive.

#### **CHAPTER: Three**

##### **Option 1: Methodology normalising reconciliation of R1 to R3 settlement runs ('CE methodology')**

We believe this methodology is fundamentally flawed. No account is made of the exceptional low level of losses CE saw in years 2005/6 and 2006/7. The later corrections and therefore higher losses after any compensatory adjustments should balance the errors of understatement of units in those years, where CE experienced gains under the losses incentive. If these low level of losses are due to activity attributable to CE then we would like to see evidence to that fact. CE stated at the workshop in December that the new incentive was

flawed as they would see windfall gains due to the methodology despite making no changes to network efficiency, we would suggest this is what has happened in previous years.

#### **Treatment of Negative EACs**

We believe this is an unnecessary adjustment. The CE methodology uses the P222 report to try and ascertain erroneous negative EACs. This report is not fit for purpose as it was designed predominantly for IDNOs to monitor activity on their Networks. It only gives a snapshot of the EACs and AAs used at the time of the report it does not give a start date for that EAC. We have done some analysis on the MPANs that were used in the CE adjustment and our sampling shows that all were removed before the data crystallised in settlement. CE has made the assumption in using November 2010 P222 report that sites all will have reached R3. This is not the case and ENWs use of later reports shows that much more volume is corrected than CE has. Ultimately we believe the adjustment is unnecessary and does not also account for any erroneously large EACs either.

#### **Option 2: Methodology normalising reconciliations for all settlement runs ('SP methodology')**

We believe this probably is the more robust methodology although we still have concerns over how a normal period is measured. Neither methodology seeks to identify the actual level of losses but merely to compensate for adjustments to data that were incorrect in previous years in which they had the benefit. Either way the customer is ultimately paying for an incentive that is fundamentally flawed.

**Question 1:** Do you agree with the general principles and constraints we have identified with respect to the correction of data used for the losses incentive scheme?

No, as no effect of the extremely low losses in previous years has been taken into account. To be fair to consumers these need to be reopened and rebalanced as well if we are to adjust years of reporting high losses.

**Question 2:** Do you think we have identified the only two practical methodologies for normalising losses incentive data for 2009-10? If not, what other approaches do you think we should consider?

No. We do not believe there is a normal data period. The whole incentive is not fit for purpose and should be

reopened.

**Question 3:** Do you agree that Options 1 and 2 are distinct approaches such that a hybrid incorporating the best points of each is unachievable?

We agree no hybrid is possible.

**CHAPTER: Four**

**Question 1:** Have we identified the important strengths and weaknesses of each option? If not, what additional points should be considered?

Please see our points above as to the weaknesses of each methodology.

**Question 2:** Do you think that the impact of particular factors on SF data can be clearly identified? Can a recessionary impact be separated from other factors such as extreme weather? How important is it for the purposes of the adjustments methodology to also take account of other variables affecting SF data such as extreme weather conditions?

These are extremely complicated factors and should have no bearing on a losses incentive scheme. The fact that we may need to consider such areas shows that the scheme is not fit for purpose.

**Question 3:** Do you consider that both methodologies can deal equally well with all types of settlements data correction?

No both are wholly inadequate and unnecessary.

**Question 4:** Should Option 2 allow DNOs to select different „normal“ periods or is there a case for setting a standard period? What would the benefits or drawbacks be of selecting a standard „normal period“ across all DNOs? Would the selection of different „normal“ periods substantially affect the outcome?

We do not believe it is possible to identify a normal period. The problem is that the incentive has been set against targets that are wholly inappropriate.

**Question 5:** Do you support our preferred approach to have a single methodology that would be used across all DNOs that

have adequate evidence of abnormally high settlement data corrections?

We do not believe either methodology should be used. Both are inadequate as they do not look at abnormally low periods of Settlement adjustment and do not address the real issue that the Losses incentive scheme is fundamentally flawed.

**Question 6:** Do you consider that Option 1 should be that single methodology? If not please give reasons for your response.

No neither option although Option 2 seems to be more sound than option 1.

**Question 7:** Are suppliers still undertaking significant levels of settlement data adjustments? What has been the impact of the changes to the BSC to limit the use of Consultation on regulatory measures to address the effects of gross volume correction and other settlements data adjustments on the distribution losses incentive mechanism GVC, and what will be the impact of P274? Are ongoing settlement data adjustments likely to be on the same scale as those observed for 2009-10?

We expect to continue the legitimate correction of settlement data as long as is necessary. Should P274 be accepted we will see a fall in the over accuracy of Settlement and prevent the adjustment of units that have been distributed. This will include the entry of stolen units that have been identified that DNOs are seeking us to enter into settlement under the DCUSA and the BSC to improve the losses incentive position. The roll out of Smart metering is likely to identify a number data errors that may need to be adjusted to correct settlement.

#### **CHAPTER: Five**

**Question 1:** Do you agree that in calculating the LRRM, the selected adjustment methodology should be applied to the 2009-10 losses reported under both the DPCR4 and DPCR5 methodologies?

No the whole incentive mechanism should be looked at as it is wholly inadequate. We are not in a position at this stage to know if P274 will come into effect nor have we looked at the increase of customers with on site generation spilling onto the network.

**Question 2:** Do you believe that either Option 1 or Option 2



could be applied to the 2009-10 losses re-reported under the DPCR5 common reporting methodology?

**Question 3:** Do you agree that in setting the DPCR5 ALP we should not include any settlements data adjustment? This is flawed adjustments will continue to happen. We would also like to know how customers with on site generation and spilling onto the network will be treated as this will artificially reduce network losses.

**Question 4:** Do you believe that the type of adjustment (GVC, DMX or other) impacts how the targets should be calculated? If so, how should this be done?

No targets should be set that are realistic and achievable from improvement in Network losses. Any adjustments that are designed to approve settlement data should have no bearing on a losses incentive.

Please feel free to contact me if you wish to discuss this response. This response is not confidential.

Yours sincerely

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