

Summary of responses – consultation on regulatory measures to address the effects of gross volume correction and other settlements data adjustments on the distribution losses incentive mechanism

Consultation Responses Summary Document

Publication date: 9 March 2012

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Overview:

Electricity Distribution Network Operators (DNOs) are incentivised to reduce losses on their networks through the Distribution Losses Incentive Mechanism. Their losses performance is measured using settlements data from the balancing and settlements system. Abnormal levels of corrections to this settlements data were observed in 2009-10, predominantly as a result an activity known as Gross Volume Correction (GVC), and which appears to have reduced some DNOs reported losses positions.

Following a number of DNO requests to restate their losses position, Ofgem issued a consultation on how to address the effects of this correction activity. This document summarises responses received to that consultation. For more background and detail of the issues raised, please refer to the consultation (see Associated documents, below).

Overall, 15 responses were received, including from six DNOs and five. This document does not seek to cover the detail of every response; nor should it be taken to reflect the views of Ofgem. No further response is requested to this document. Full copies of responses are available, alongside this summary, with text redacted as appropriate.

Associated documents

Consultation document on data cleansing and GVC (Ref 137/11)

<http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=607&refer=Networks/ElecDist/PriceCtrls/DPCR5>

Consultation on implications of gross volume corrections for DNO revenues; 20 July, 2010 (Ref 87/10)

<http://www.ofgem.gov.uk/Networks/ElecDist/Policy/Documents1/Consultation%20on%20implications%20of%20gross%20volume%20corrections%20for%20DNO%20revenues.pdf>

Authority decision on relief from the consequences of over-recovery of allowed revenue caused by GVC in settlement data; 14 December, 2010

<http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=54&refer=Networks/ElecDist/Policy>

Decision on CE request to restate losses info for 2009-10; 17 December, 2010

<http://www.ofgem.gov.uk/Networks/ElecDist/Policy/Documents1/Decision%20on%20request%20from%20CE%20Electric%20UK%20to%20restate%20losses%20for%202009-10.pdf>

Open letter: Consultation on the way forward in dealing with the interactions between the electricity distribution losses incentive scheme and Gross Volume Correction (GVC) activity; 21 March, 2011 (Ref 35/11)

http://www.ofgem.gov.uk/Networks/ElecDist/PriceCtrls/DPCR5/Documents1/OpenLetter_GVC_impact_on_DNO_losses_incentive_Mar11_Final.pdf

Information on responses to consultation on the way forward in dealing with the interactions between the electricity distribution losses incentive scheme and Gross Volume Correction (GVC) activity; 24 May, 2011 (Ref 70/11)

<http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=555&refer=Networks/ElecDist/PriceCtrls/DPCR5>

Interim decision on ENWL request to calculate distribution losses for 2009-10 on a basis that differs from that used for 2002-03; 29 July, 2011

<http://www.ofgem.gov.uk/Networks/ElecDist/PriceCtrls/DPCR5/Documents1/Interim%20decision%20on%20request%20from%20ENWL%20to%20restate%20losses%20for%202009-10.pdf>

Electricity Distribution Price Control Review Final Proposals – Incentives and Obligations; 7 December, 2009 (Ref 145/09)

http://www.ofgem.gov.uk/Networks/ElecDist/PriceCtrls/DPCR5/Documents1/FP_2_Incentives%20and%20Obligations%20FINAL.pdf

Electricity Distribution Price Control Review Final Proposals – Financial Methodologies; 7 December, 2009 (Ref 148/09)

http://www.ofgem.gov.uk/Networks/ElecDist/PriceCtrls/DPCR5/Documents1/FP_6_DPCR5%20Financial%20methodologies.pdf

DPCR4 Elec Distribution Price Control Review - Final Proposals; 28 Nov 04 (265/04)

<http://www.ofgem.gov.uk/Networks/ElecDist/PriceCtrls/DPCR4/Documents1/8944-26504.pdf>

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1. Headline messages

Chapter Summary

This chapter summarises some of the points made in the summary notes or cover letters accompanying responses to the consultation.

Responses summary

- 1.1. Key points drawn out in consultation response cover notes included high level issues to do with losses and data cleansing activity generally, as well as concerns with each of the methodologies.
- 1.2. At the highest level, a number of responses reiterated concerns made previously that settlements data was not designed for use in measuring losses and called for further consideration of the approach to incentivising losses reductions across electricity distribution networks.
- 1.3. But, while responses did not dispute the existence of data cleansing activity, they did question the justification for, and the materiality of, restatement of reported loss positions. One of the reasons put forward was the importance of protecting consumers from unfair or sudden increases in bills. Such comments were supported by responses which questioned whether errors being corrected for in 2009-10 had originated earlier within the fourth price control (DPCR4) period, meaning that DNOs may have already received the benefit. In line with these points and comments on the appropriateness of settlements data, concern was also raised about the very low level of losses performance at points during the DPCR4 period in some licensee areas.
- 1.4. However, there was equally good support for the need to address abnormal correction activity. In particular, such comments highlighted the need to ensure that reported losses in 2009-10 reflected absolute losses performance across the period, stating that not restating the corrections would be inconsistent with the way in which the DPCR4 targets were set.
- 1.5. Responses to the consultation also highlighted that correction activity is not uniform, referencing a variation in the timing, intensity and type of correction activity. This variation was one reason why some responses suggested that selection of a “normal” period was difficult, and why DNOs should be able to select their own normal period. However, responses also suggested that the reason selection of a normal period was difficult was because of the volatility of settlements data itself and was something that had been signed up to in accepting the DPCR4 price control settlement. These responses suggested that where it was not possible to identify a clearly abnormal period, restatement of 2009-10 reported losses to address correction activity should not be permitted.



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- 1.6. A number of responses questioned whether all of the different types of data correction activity had been properly considered. However, none were able to identify means of separating out, for example, GVC from DMX (dummy meter exchange) correction activity. Similarly, a number of respondents commented on the importance of reflecting the impacts of extreme weather or the recession. However, it was also highlighted that the losses mechanism itself does not make specific reference to the impact of weather, short of allowing for profiling of the SF (Initial Settlement) position; and isolating the specific effects was difficult.
- 1.7. In considering the detail of the methodologies, a number of responses had concerns with the treatment of negative EACs (estimate annual consumption) under the CE methodology. They highlighted that the volume of energy associated with data correction is unlikely to be the same as the negative EAC values considered by the methodology. These comments were supplemented by concerns with the P222 report, that EAC values in the report were not linked to a run type. Responses also commented that some DNOs did not have historic copies of the report, making the CE methodology difficult to replicate. There were a number of responses which supported the CE methodology however, particularly referencing its transparency and workability.
- 1.8. This relative simplicity was considered to be an advantage over the SP methodology. With respect to the SP methodology, a number of comments were also made criticising the level of influence and involvement of the DNOs, referring to the lack of criteria and level of subjectivity in selection of a normal period. However, the ability to select a normal period was itself considered a fundamental benefit by many. A number of responses also suggested that the SP methodology was more robust and dealt better with the correction activity than the CE method.
- 1.9. Looking forward to the fifth price control (DPCR5), a number of responses suggested that data correction activity was ongoing, though not to the same extent as for 2009-10. The majority of responses also highlighted the importance of being prepared for the roll out of smart metering and recognising the impact such activity would have on settlements data.

2. Detailed answer summary

Chapter Summary

This chapter provides a breakdown of responses to specific questions asked in the consultation along with a summary of some of the supplementary points made. Even where questions allowed for a “yes/no” answer, not all responses were explicit or provided one. Numbers of respondents in each category should therefore be seen predominantly as a guide, and should not be taken as a substitute for full responses. Where a number of questions were asked at the same time, a breakdown is provided where it is helpful to do so.

Chapter 2 - Settlement data adjustments and their impact

Response breakdown

	Yes	No	Other ¹
Question 1: Do you think we have identified the main data/billing adjustment techniques used by electricity suppliers and their impacts?	8	1	6
Question 2: Are there any other factors you think we should take into consideration in assessing the impact of settlement data volatility?	Breakdown not possible		

Summary of response breakdown and supplementary points

- 2.1. Of note is that the significant majority of respondents answering clearly felt that the main data/billing adjustment techniques used by electricity suppliers had been identified. However, it was suggested that there may be other factors affecting movements in settled meter volumes. These included increased number of actual meter readings going into settlements and correction of erroneous data.
- 2.2. In answer to Question 2, responses highlighted the importance of considering fairness for consumers, particularly the vulnerable, in terms of cost per household as well as the value per tonne of associated carbon dioxide emissions. It was also suggested that thresholds of materiality should be set for future methodology change applications.

¹ “Other” includes those who provided no answer or provided no clear “Yes” or “No”.

- 2.3. In considering the timing of corrections activity, it was commented that 2009-10 was in the middle of a recession so it was reasonable to assume that some AAs (annualised advances) would be legitimately lower than EACs (eg as a result of increased theft or large consumers operating at lower levels). Respondents also highlighted the impact of errors in earlier years being corrected in 2009-10. Some suggested that if 2009-10 restatement was permitted, other years where DNOs have accepted benefits of overstatement should also be reopened. It was also suggested that if a large number of downward corrections were taking place, an increased variation in Grid Supply Point Group Correction Factor between settlement runs would be visible.
- 2.4. In considering the settlement corrections themselves, it was suggested that some correction activity was as a result of the receipt of late or incomplete data from DNOs.

Chapter 3 - Normalisation of 2009-10 settlements data

Response breakdown

	Yes	No	Other
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?	9	2	4
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?	7	5	3
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?	9	0	6

Summary of response breakdown and supplementary points

- 2.5. Of note, is the high proportion of respondents agreeing with the general principles and constraints identified, as well as that Option 1 and 2 are distinct approaches and that a hybrid approach is not achievable.
- 2.6. Of those responses answering “no” to Question 2, points made include that the volatility of settlements data throughout DPCR4 means that DPCR3 would be more appropriate for selecting the normal period. A number of responses also suggested that as a result of there being no normal period and both methodologies only focussing on high losses, neither methodology should be

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used. More broadly, some responses asserted that it was not appropriate to restate for GVC activity at all.

Chapter 4 - Comparison of Options 1 and 2 and our preferred way forward

Response breakdown

	Yes	No	Other
Question 1: Have we identified the important strengths and weaknesses of each option? If not, what additional points should be considered?	6	6	3
Question 2a: Do you think that the impact of particular factors on SF data can be clearly identified?	2	8	5
Question 2b: 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?	0	7	8
Question 3: Do you consider that both methodologies can deal equally well with all types of settlements data correction?	4	7	4
Question 4a: 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?	8	1	6
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?	8	5	2
Question 6: Do you consider that Option 1 should be that single methodology? If not please give reasons for your response.	4	6	5
Question 7a: Are suppliers still undertaking significant levels of settlement data adjustments?	2	5	8
Question 7b: What has been the impact of the changes to the BSC to limit the use of GVC, and what	Breakdown not possible		

will be the impact of P274?			
Question 7c: Are ongoing settlement data adjustments likely to be on the same scale as those observed for 2009-10?	1	4	8

Summary of response breakdown and supplementary points

- 2.7. Notwithstanding those responses that agreed with Ofgem's assessment of the strengths and weaknesses, most respondents either reiterated salient points or raised new issues.
- 2.8. In considering the CE methodology, it was suggested that:
- the approach to discarding the RF (Final Reconciliation) and DF (Dispute Final) data is flawed, potentially treating "normal" variations as "abnormal". Comments suggested that it does not seem appropriate to ignore RF-DF data given that most of the meter readings, and hence AAs, will be obtained between R3 and RF. Though it was also noted that about 8 per cent of the metering systems settled on AAs at RF during 2009-10 had been read (or processed) since the R3 (Third Reconciliation) run. Respondents also felt that this approach ignores the impact that negative EACs will have had on earlier run types, including SF, until such time as they were replaced by AAs.
 - the whole concept of making an additional adjustment to data where a top down correction has already been applied is flawed and should not form part of any methodology.
 - the use of a fixed normal period was considered to be a concern by many. It was additionally noted that the 'observable' data being used for the normal period is likely to be the years in which the original errors in settlement occurred, therefore there is an inherent flaw in using these years to 'normalise' the year which corrects them.
 - the treatment of negative EACs was a concern (this was true for many of the respondents). One of the key reasons highlighted was that the approach taken was not an appropriate means of identifying the level correction activity that was abnormal or as a means of quantifying the volume of energy that had been corrected. Respondents felt that adding in a set of negative EACs was illogical and that monitoring of them would prevent consistent treatment by all DNOs.
 - similarly, the use of P222 reports was a concern because of only being available on request (this would make it very difficult for some DNOs to

implement). But even when available, it was stated that they do not provide a complete picture of the extent to which any negative EACs had an impact on settlement volumes. Comments highlighted the fact that no account is taken of the settlement day and run type at which the negative EAC began to impact settlement data volumes or of the settlement day and run type at which the negative EAC ceased to impact settlement data volumes. Also in relation to the P222 report, it was highlighted that one DNO is using a more up to date version of the report than another for monitoring corrections, which results in different levels of restatement.

- a number of comments were also made about the lack of treatment of positive EACs in the CE methodology.
- the methodology was both transparent and workable (an important strength), and would require minimal input from DNOs. In addition, the monitoring requirements are straight forward and easily demonstrated.
- the CE method is firmly grounded in a dataset (ie the SF run) over which the distributor has no influence and does not require any subjective judgement to be made by the distributor or Ofgem about the starting dataset.

2.9. In considering the SP methodology, it was suggested that:

- allowing DNOs to choose their own normal period was a concern, particularly since it is not an appropriate basis for consumers to fund the close out of the DPCR4 losses incentive. Comments suggested that what the consultation stated was a 'statistically modelled approach' amounts to looking at a graph and identifying a period where the graph looks relatively flat. This meant the classification of the normal period was highly subjective and could differ between DNOs. This could mean that each DNO's assumptions around the choice of the normal settlement period would be based on each DNO's observed patterns, and in doing so, it could lead to a DNO choosing a period which gives it the most favourable result.
- as with the CE methodology, an additional concern with the choice of normal period was that the period needed to be different to the one in which the erroneous data occurred.
- the SP methodology was probably more robust, though it was similarly noted that 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.
- the correction methodology comes from different reconciliation runs and is less reflective of supplier activity.

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- it was less transparent and more complex to apply, however, it was also noted frequently that the ability to choose an network specific normal period was a strength (provided the DNO had sufficient justification).
 - argument about extreme temperatures were spurious. This is because the method uses profiled data (and so reflects temperature variations to the same extent that settlements does). But also that the losses incentive itself does not attempt to model the relationship of losses with the current, hence this is a level of detail that goes beyond either methodology.
- 2.10. In addition to the points made above at paragraphs 2.8 and 2.9, those that did not agree that Ofgem had identified the important strengths and weaknesses highlighted that GVC also creates losses reporting anomalies prior to 2009-10, which may warrant the ability to look for normal periods within the third price control (DPCR3) period.
- 2.11. Looking at the additional questions in Chapter 4, of note is that a significant majority felt that the impact of particular factors on SF could not be clearly identified or separated.
- 2.12. Those respondents suggesting that both methodologies did not deal well with all types of data corrections did so in part to reinforce concerns raised in respect of the CE methodology – especially in relation to discarding of the RF-DF data and the treatment of negative EACs.
- 2.13. The majority of respondents supported the approach of having one single methodology, though commented that this should not be at the expense of achieving the right answer. The importance of understanding the impact on consumers was also noted.
- 2.14. Key points to note in terms of those in favour of Option 1 or Option 2 were that:
- those in favour of Option 1 included two DNOs who have received interim decisions in favour of restatement. Of the two additional respondents in favour, one highlighted that most of the DPCR4 period was abnormal and that the normal period should be chosen from DPCR3.
 - of those in favour of Option 2, two were the DNO suggesting the option and the organisation having developed it. Of the additional four respondents, all were suppliers.
- 2.15. In considering whether data cleansing activity was ongoing, a number of DNOs felt that it was, though perhaps not to the same extent as was seen in 2009-10. There were many comments about the impact that smart metering might have on settlements data going forward.

Chapter 5 - Interaction with the losses rolling retention mechanism and targets for DPCR5

Response breakdown

	Yes	No	Other
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?	4	5	6
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?	3	2	8
Question 3: Do you agree that in setting the DPCR5 ALP we should not include any settlements data adjustment?	7	4	4
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?	4	4	7

Summary of response breakdown and supplementary points

- 2.16. A variety of opinions were put forward in respect of Chapter 5 and how adjusted data should be taken account of in the LRRM and the DPCR5 ALP. Comments were driven by decisions on the approach to adjusting for settlements corrections, as well as whether corrections activity was ongoing. Of note however, is that the majority of respondents agreed that the DPCR5 ALP should not include any settlements data restatement. There was also support for the principle that the LRRM should be self contained, minimising any interaction with DPCR5 where possible.
- 2.17. Looking ahead to DPCR5, it was noted that the extent to which supplier correction activity is ongoing will dictate whether further requests for restatement of losses performance are required.
- 2.18. Respondents also commented on the distinction between GVC and DMX or other types of settlement corrections activity noting that, while the type of correction may have an impact, it was not possible to distinguish between them.