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Sent via email to joanna.campbell@ofgem.gov.uk

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Dear Ms Campbell

Ofgem Consultation – Reference 52/12
Mitigating network charging volatility arising from the price control settlement

I am writing to set out Haven Power Limited's views on your network charging volatility consultation. We have included answers to specific consultation questions in Annex 1 of this letter.

Haven Power Limited ("Haven") is a non-domestic electricity supplier and has been part of the Drax Group plc since 2009. We began supplying the SME (Small Medium Enterprise) sector in 2007 and now have ~38,000 customers. In 2009, we entered the I&C (Industrial & Commercial) sector and have grown our customer base to ~1,000.

Since the start of the year, we have discussed our concerns in relation to network charging with the Ofgem team several times and see this consultation as a positive step forward. However, we believe that it is too narrow in focus.

The price control settlement is only one source of volatility in network charging and all factors should be taken into consideration when considering any measures to reduce the level of movement in these charges. For example, the models used (inputs, algorithms etc.) to calculate network charges and the cost reflect nature of the methodologies also give rise to volatility and this is often bigger than the volatility caused by the factors that you have included in your consultation.

We firmly believe that Ofgem needs to consider the issue of network charging volatility "in the round". This will ensure that any actions taken to reduce it are only implemented after a full consideration of all the issues and that the risks identified are placed with the party best able to manage them. Limiting the debate and any associated actions to one cause may only exacerbate volatility arising from another factor.

The uncertainty in the level network charges can be significant and recent year-on-year variations have been significantly higher than the level of gross margin a supplier could expect to achieve in this market sector. New entrant / independent suppliers tend to operate in niche market sectors and do not have a diverse portfolio over which variation in costs can be absorbed. We are sure you will agree that the current environment is not favourable for encouraging new entrants into the market or for allowing existing smaller / independent players to grow.

As a result of our concerns, we have raised modification proposals under both the CUSC and DCUSA industry codes to require NWOs to provide more information on future network charges and to limit year on year increases to 20%. These are currently being assessed by industry working groups.

We are in the process of arranging to follow up further with Hannah Nixon in relation to network charging volatility, but if you require any further information in the meantime, please get in touch.

Yours sincerely

Sent by email.

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Annex 1
Mitigating network charging volatility arising from the price control settlement
Consultation Question Answers

Question 2.1: Have we correctly characterised the scope of the problem we are trying to address?

We agree that the lack of predictability of network charges is a major area of concern for suppliers. It is therefore right to focus on implementing solutions to make network charges more predictable. However, it is also the case that the volatility of charges itself is an area of major concern for suppliers (as demonstrated by the very large price movements seen year on year. Please see our answer to question 2.2 for some examples of very significant price movements). Such price movements can damage consumer confidence in the supply market which is likely to deter proactive customer engagement with the supply market. Ultimately, this might result in a less competitive and efficient energy market.

In addition to volatility arising from the price control settlement, we believe that Ofgem needs to consider volatility in network charges "in the round". There are other causes of volatility – for example, the CDCM (Common Distribution Charging Methodology) model appears to be very sensitive to even small changes in input parameters and the methodologies themselves. Considering only one source of volatility may be of limited value as any benefits may be masked by the volatility caused by other parameters in network charge calculations.

Question 2.2: Are there certain market segments or groups of customers that are particularly affected by charging volatility?

Your consultation document focuses on cost to domestic customers, but it is important to remember that all customers pay network charges and small and large businesses are affected too.

We do not believe that it is possible to say with any certainty that there are particular groups of customers that may be affected by charging volatility in the future. Between 2011/12 and 2012/13 we saw a number of double digit increases in DUoS tariffs and unpredictable movements at the tariff component level. For example:

MANW	*HH*	*HV*	*Amber Rate +256%*
YELG	*HH*	*HV*	*Green Rate +91%*
NEEB	*PC5-8*	*LV*	*Unit Rate 2 +60%; and*
SOUT	*HH*	*LV Sub*	*Red Rate +47%, Amber Rate -73%*
LOND	*HH*	*LV Sub*	*Fixed -13%, Amber +13%*
SOUT	*PC4*	*LV*	*Unit Rate 1 +51%, Unit Rate 2 -47%*

Large increases and volatile movements such as these mean that suppliers (particularly new entrant / small suppliers who are often active in only one market sector), may be particularly exposed to future network charges. As a result, customers may be adversely affected if suppliers are forced to include additional risk premia in their retail prices because of the uncertainty in network charges.

Question 2.3: Do you agree with the assessment criteria? Are there additional criteria that we should adopt for our final assessment?

In our view it is important that any measures put in place ensure that the risk is placed on the party best able to manage it, are simple and fit into the RIIO framework. This would help to ensure that the cost to consumers is kept to a minimum.

Question 3.1: Do you have any further suggestions of what could be done to mitigate network charging volatility arising from the price control settlement?

Ensuring that NWOs fulfil their obligation to offer fixed network charges for longer than one year and across yearly boundaries.

Question 3.2: Do you agree with our initial assessment of each option?

We feel that a cap on changes would be beneficial. It would begin to introduce some certainty over the maximum year on year increase. This would be beneficial for customers as suppliers will have a firm basis for the maximum level of any risk premia they include in their retail prices. We have raised modification proposals under both the CUSC & DCUSA to introduce a cap on year on year charge increases.

Option 1: Improved information provision

Question 3.3: Do code and licence charge notification differences in each network sector create problems in managing charge changes?

Yes. There are differences between the CUSC and DCUSA in relation to the provision of information relating to network charges. For example, there are different notice periods for advising suppliers of changes to transmission and distribution network charges and this affects when changes to charges can be factored into suppliers' retail prices. Standardization would allow for all charges to be dealt with at the same time. There are also differences in the level of detail of charging information provided; we have raised modification proposals under the DCUSA and CUSC to improve the detail and increase the frequency of information provided by NWOs.

Question 3.4: What information would you like the network operators to provide, that they currently do not, in order to help improve predictability of network charges for different customer groups? This should include:
a) what information you would like to see in their business plan submissions, and
b) what information you would like to see provided on an ongoing basis.

We would like to see network operators provide regular updates of future charging information at the level provided in their Use of System Charging Statements for at least the year following the one for which final charges are published. We have raised code modification proposals to require network operators to do this and they are currently being assessed by working groups. We expect the timing of within year updates to reflect key changes in data used in the charge calculations.

Question 3.5: What information do you think we could provide that the network operators cannot, that would benefit you in terms of improving predictability of network charges?

In relation to transmission network charging, we believe it is important that Ofgem facilitates the sharing of regular information relating to allowed revenues between OFTO / other TOs and NGET to allow regular and easy updating by NGET of transmission network charges.

Additionally, we believe Ofgem should revisit the timing of agreement of allowed revenues for TOs and SOs under the relevant schemes (although we note that SO incentive schemes are not within the scope of this consultation). This is particularly important at scheme boundaries and anything less than 12 months is not sufficient as NWOs will not be able to provide the best view of future charges for suppliers to factor into their retail prices.

Option 2: Restricting the frequency of intra-year charge changes

Question 3.6: In the last five years how frequently have networks introduced intra-year changes? What were the main reasons for these changes?

Question 3.7: Are there any business processes that would mean only allowing one change per year on 1 April would not be feasible?

We are not aware of any external business processes in the electricity sector that would make one change each year on 1 April unworkable.

Restricting changes to once each year would be a positive step for all suppliers, but particularly for smaller players and new entrants were resources can be limited. This would remove this as a potential barrier to market entry / growth.

Question 3.8: Do you think that there should be exemptions that would allow for changes due to specific events? Do you think these events should include the occurrence of errors when calculating charges or changes to the charging methodologies? Are there any other events that should potentially be exempt?

Any situations where intra-year charge changes were allowed would need to be carefully defined to avoid disputes over whether a NWO's proposal for a change to network charge is valid or not.

We do not believe that when a NWO has made an error it should be allowed to make an intra-year change to network charges. Very few customers (we only envisage that large consumers on pass-through arrangements) are likely to be immediately impacted (positively or negatively) if changes arising from calculation errors are passed on to suppliers as it will not always be possible or practical for a supplier to increase charges to customers as a result of the change made by the NWO. The supplier will win or lose.

Question 3.9: Do you agree with our proposed change to the penalty for over or under recoveries were this option to be implemented?

Question 3.10: Do you agree with our initial view that there should be a two year lag on adjustments due to the over or under recovery of revenue through the correction factor?

We believe that this would reduce volatility and so we would support this.

Question 3.11: Are you aware of any errors that have been made when calculating network charges in sectors other than electricity distribution?

Question 3.12: Do you think that introducing an additional licence condition to penalise NWOs when they make charge calculation errors is warranted?

We are in favour of lighter regulation across the industry. If NWOs are correctly incentivised, then an additional licence condition should not be required.

Option 5: Imposing a cap and collar on allowed revenue changes

Question 3.16: Do you agree or disagree with our initial assessment that the benefits of introducing one of the three options for a cap and collar do not outweigh the drawbacks?

We have raised modification proposals to limit year on year changes in electricity network charge tariffs and these are being considered by industry working groups. These will explore how our proposal could be implemented. We believe that cap and collar arrangements are appropriate and the benefits across the industry and for customers would far outweigh the costs.

Question 3.17: Do you consider there are any other options for the design of a cap and collar mechanism that we have not considered?

See above.

Question 3.18: Do you have any views on whether a cap and collar, if implemented, should be symmetric or asymmetric?

We believe providing a check on the maximum level of increase in network changes is key to aiding suppliers and customers in the long-term and our modification proposals are asymmetric and do not seek to place any restriction on any reductions in network charges.

Timing of implementation

Question 3.19: Do you agree that if changes are needed in the gas distribution or transmission sectors that they should be implemented on 1 April 2013, the start of the next price control period?

Yes, we believe that any changes needed should be implemented as soon as possible.

Question 3.20: When should we apply any changes to the electricity distribution sector?

The next electricity distribution price control doesn't start until April 2015. We believe any changes should be implemented as soon as possible even if this is before the start of the next price control. It is critical that suppliers have certainty on distribution charging as quickly as possible and ideally two years ahead of the relevant year. We believe that this should be factored into the implementation of the price controls.