OVERVIEW DOCUMENT:

CONSULTATION ON STRATEGY FOR THE NEXT ELECTRICITY DISTRIBUTION PRICE CONTROLS

CHAPTER: Three

Question1: *Do you have any comments on our stakeholder engagement approach?*

We are disappointed that there has not been an Ofgem-led forum for suppliers to input directly into the RIIO-ED1 process. The current process relies on individual DNOs doing their own stakeholder management with suppliers. Not only is the quality likely to be more variable, it also means that it is more difficult to get views of suppliers incorporated into the overall RIIO-ED1 process.

Ofgem RIIO ED1 working groups where RWE has participated have been useful in enabling us to engage in responding to this set of consultations. They have been well organised and have enabled stakeholders to have an insight into DNO's views and to pose questions to Ofgem and DNOs.

Question 2: *Do you have any views on how our engagement process or that of the DNOs could be made more effective?*

In some instances, stakeholder engagement needs to be more focussed, targeting similar groups as opposed to more generalised stakeholder engagement. For example, suppliers will require very different types of information to other stakeholders. A more focussed view on actual stakeholder types and their individual needs would be advantageous.

We would urge Ofgem to consider the requirement for a separate working group for suppliers, thereby facilitating full and consistent engagement in the RIIO-ED1 process.

For non-DNO stakeholders that are new the engagement process an initial workshop to introduce the background and historical development of the price control may enable them to participate more effectively.

CHAPTER: Four

Question1: *Do you have comments on the form or structure of the price control?*

As per our comments above, we believe the price control should also focus more on the needs of suppliers, and in particular, be set up to provide more transparency and predictability of charging.

DNOs are being asked during to provide their plans for 8 years. There should be an overall commitment to the agreed numbers. Re-openers or uncertainty mechanisms should be minimised and appropriate delays built into the implementation in order to provide transparency and predictability of revenues for suppliers and consumers, as well as the avoidance of price shocks. If such re-opener / uncertainty mechanisms are the 'norm', it weakens the concept and effectiveness of a longer term price control.

Question 2: *Do you agree with our proposed changes to the RIIO-ED1 timetable?*

We are comfortable with an 8 year price control. We are, however, not comfortable with the timing of information provision to the market. Final Determination in February or November 2014 is too late for the Retail Market in terms since many contracts will have been agreed between suppliers and consumers spanning April 2015 by then.

Question 3: *Do you have a view on the materiality of potential changes in allowed revenues/charges between price controls? Do you have proposals to address this?*

We do not have any view at the moment on the materiality of potential changes in allowed revenues /charges between DPCR5 and RIIO-ED1. This will not be known until November 2014 if DNOs are not fast tracked or February 2014 if DNOs are fast tracked. This causes a commercially unviable issue for suppliers since the extent of the revenue step change between price controls will not be known until very late on in the process.

The uncertainty and issues in the market caused by such late revenue notification timescales can easily be demonstrated by RIIO T1/GD1, which follows similar timescales to those proposed for RIIO-ED1. For example, in April 2012 National Grid published their best view illustrative tariffs, based on their view of 2013/14 business plan revenues. In November 2012, they have updated this view, based on their latest view of data. NGET's forecast of TNUoS demand tariffs have decreased (up to £3.47 /kW for half hourly and 0.47p/kWh for nhh tariffs). Much of this forecast tariff decrease is driven by a change in NGET's forecast revenue for 2013/14 (£293m reduction). Even in November 2012 there is still considerable uncertainty around tariffs. NGET have stated that *'it should be noted that the total transmission allowed revenue remains subject to change as the RIIO-T1 process continues and as Ofgem develops the detail licence drafting to implement the price controls'.* This uncertainty around allowed revenue and step change due to price control makes is at odds with Ofgem's recent consultation to improve transparency and predictability of Network Charges.

We would suggest the following options to overcome the late notice of revenues to suppliers.

1 The current timetable is revisited to publish all Distribution Network Operator (DNO) Final Allowed Revenues much earlier than intended.

2 Fix Allowed Revenue numbers for each DNO for 2015/16 and 2016/17 early. Changes to those initial numbers as a result of the ongoing RIIO-ED1 review process by Ofgem will still be recovered by DNOs but spread across future (post April 2017) years using the 'k factor' (a standard price control process);

3 Implement a narrow cap and collar (say +/-5%?) around an early published allowed revenue for each DNO for 2015/16 and 2016/17 and apply any further over or under recovery as per option 2.

This revenue certainty should be provided by **March 2013** at the latest, thereby providing suppliers with greater certainty around the level of DUoS tariffs in the 2 years leading up to RIIO-ED1. Suppliers contract with larger consumers on a 1, 2 and 3 year basis. Many of these contracts will be 'fixed price' where the DUoS charge is incorporated into the overall unit rate(s) and fixed charge that the customer sees on their invoice. Suppliers' ability to forecast DUoS tariffs accurately over that time horizon is key to ensuring that the consumer is given the most cost reflective price.

CHAPTER: Five

Question1: *Do you consider that the proposed outputs and associated incentive mechanisms, taken together with other elements of the price control, will ensure that companies deliver value for money for consumers, and play their role in delivering a sustainable energy sector?*

We consider it important that outputs and associated incentive mechanisms need to be set at the appropriate level. Incentives should only be payable for performance above and beyond the norm. Payments should not be made to simply meet a 'reasonable standard'. Standards should be set at the higher end and penalties applied if not met. We believe that Ofgem are best placed to identify where and how these incentives are set to ensure that DNOs deliver value for money for consumers and play their role in delivering a sustainable energy sector.

Question 2: *Do you consider that the proposed outputs and incentive arrangements are proportionate (e.g. do we have too many or too few)?*

Question 3: *Do you have any views on the proposed outputs and incentives?*

DG Related incentives

- **Removal of the 'DG incentive'**

We accept the feedback that the DG incentive has not worked successfully in the past in achieving intended outputs, that it can lead to perverse behaviour on part of the DNOs, and that it has been underutilised. On this basis there is no justification for retaining it in its current form. However, the original rationale for having a measure that "significant uncertainty around the volume of DG that will connect (in DPCR5), its generation type, location and voltage, all of which make it very difficult to anticipate the cost of connecting the DG to the networks"[1](from DPCR5) still stands. Forecasting DG uptake as well as the uptake of a broader suit of low carbon technologies remains very difficult. This is especially so given the uncertainties around the reform of DG support via the on-going EMR consultations, changing success rates through the planning system and the challenge that DNOs need to make assumptions over extended timeframe for the coming price-control review. In light of this we are keen to understand what the alternative measure will be to ensure that DNOs can make necessary investments in face of uncertainty. We disagree that the incentives set out under 5.2 of this Strategy paper are the complete solution to this particular challenge.

The proposal that all installations of low carbon technologies delivered through a specific new or upgraded connection project should be subjected to the connections funding mechanism seems to make sense[2]. Again though it would be important for Ofgem to engage the DG community early on in the consultation process. Interpreting the RIIO-ED1 consultation and its impacts is not straightforward for customers.

[1] (DPCR5 Final Proposals - Incentives and Obligations, p15)
[2] As suggested in RIIOED1SConCostAssessment.pdf Chapter 5, section 5.10

Treating DG connections as you would other primary network connections under Network Investment[3] could also work – but we ask for clarification on how uncertainty around EHV DG connections is to be dealt with. We are not convinced that the re-opener mechanism would allow for adjustments to be made dynamically enough in the face of deviation from modelling. It is positive that DNOs will have responsibility to understand and forecast DG demand in their area and we will scrutiny the forecasting approach of DNO business plans. However Ofgem must accept that this is not an exact science. We note that LV low carbon connections (including DG) will be associated with a volume driver to help. Is there a hybrid solution that could provide responsibility for accurate forecasting and accommodate deviation in a dynamic way for EHV DG?

- **New Average Time to Connect Incentive for EHV connections**

We feel that this inventive instead of improving matters for EHV customers will instead drive DNOs to be less responsive to customer needs. The time taken from initial submission of a planning application to a project becoming operational varies significantly from project to project depending on local factors. Many factors that can delay or expedite the time to connect are outside the influence of the DNO. Therefore penalising a DNO on this basis is not justified. The measure could push DNOs to rushing to connect at a timescale that does not accommodate the customer's needs.

- **Planned outages – could there be an incentive for efficiency?**

What could be done by Ofgem to facilitate better timing and speedier planned outage works so that DG generators do not lose out on unacceptable levels of potential revenue? Currently 'efficiency' on this front is defined by each DNO, without any Ofgem guidance. The issue is that some sites have lost out on millions of pounds-worth of potential generation due to delays, ill timing, mismanagement and poor communications regarding planned outages.

CHAPTER: Six

Question 1: *Is our proposed approach to cost assessment appropriate?*

While generally supporting the concept of a fast-tracking process, we are concerned it may result in inequality in the Retail Supply market. For example, a major supplier in a DNO area that is fast tracked will have more predictability / certainty over its cost base than a major supplier in an area that has not been fast tracked. This may therefore result in consumers in areas which have not been fast tracked paying more for their energy due to risk margin having to be applied by their suppliers. This supports the need to fix the revenues at an early stage for all DNOs – as stated above, ideally March 2013.

Question 2: *Do you have views on our proposed use of proportionate treatment?*

As above.

Question 3: *Do you have any views on the criteria for assessing business plans?*

[3] RIIOED1SConCostAssessment.pdf Chapter 5

We would urge Ofgem to ensure that a consistent approach and standard format is implemented for all DNO business plans. This makes information easier to compare and ensures consistency across stakeholders who will need to interpret this information into meaningful results.

CHAPTER: Seven

Question 1*: Do you have any views on the role of innovation in RIIO-EDI?*

Innovation is an important role for DNOs in RIIO-ED1 since it should drive more efficient costs. We support the proposal that learning is shared.

Question 2: *What should the funding threshold for the NIC be? Do you agree with our proposal to review it after two years to reflect learning from the LCN Fund?*

All Innovation Revenues should be subject to a 2 year lag, in line with the principles implemented for other revenue adjustments in the volatility consultation decision document. This will improve predictability and transparency for suppliers and result in reduced levels of risk premia being required for customer contracts.

CHAPTER: Eight

Question 1: *Do you have any views on the uncertainty mechanisms identified?*

We welcome that Ofgem recognises the link between the application of uncertainty mechanisms and price volatility for Network Users and consumers. While we recognise the increased risk caused by an 8 year price control, we would urge Ofgem to ensure that uncertainty mechanisms which are unpredictable (e.g. additional revenue for reopeners) are notified and implemented with a sufficient time lag for suppliers to price into contracts. Uncertainty mechanisms should be used as the exception rather than the norm.

If the mid-review process in 2018 results in a change to DNO revenues, we would urge Ofgem to apply a sufficient lag (2 years) to increase predictability of tariffs for suppliers. The current proposal of implementing changes in April 2019 undermines the positive steps made by Ofgem in the recent Volatility Consultation decision document to increase predictability and transparency of tariffs during a price control.

Question 2: *Are there any additional uncertainty mechanisms required?*

No

Question 3: *Are there any mechanisms that we have included that are not necessary and why?*

We are concerned that the volume driver for DNOs could conflict with innovation since it encourages system reinforcement as opposed to network management solutions.

CHAPTER: Nine

Question 1: *Do you consider that our proposed package of financial measures will enable required network expenditure to be effectively financed?*

Question 2: *Do you have any views on our proposed approach to assessing the cost of equity and the associated range of 6.0-7.2 per cent (real post-tax)?*

Question 3: *Do you have any views on the other elements of our financeability proposals?*