



RIIO-ED1: Electricity Distribution Networks Operators' (DNOs) business plans

Submission by Prospect's Northern Powergrid Branch
to Ofgem

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Introduction

1. Prospect is an independent, thriving and forward-looking trade union that represents over 115,000 professional people: managers, engineers, scientists and professional specialists in both the public and private sectors. This submission only considers Northern Powergrid's business plan.
2. Prospect represents 625 engineers, managers and other professional staff employed by Northern Powergrid. We are extremely proud about the Company's reputation as it reflects on our professionalism and we are committed to working with the Company to:
 - improve customer service,
 - ensure that new connections are made safely and promptly with clear, consistent and transparent pricing,
 - maintain and improve system reliability and availability,
 - meet our commitments to sustainability as part of the national low-carbon agenda, and
 - uphold exemplary safety standards.
3. We believe that our working relationship with Northern Powergrid is very productive: whilst we disagree on details, there is agreement over the Company's strategy of providing a cost-effective and safe service whilst improving the standards of customer service. To create the environment where the Company employs sufficient staff with the right skills to meet consumer expectations, we can point to achievements such as the ground-breaking five-year pay settlement as proof of our joint commitment to develop the business to improve the electrical infrastructure vital to our region's prosperity. By focussing on rewarding skills and their delivery, Northern Powergrid has the most productive workforce of all the DNOs
4. Thus we welcomed the opportunity to comment upon and influence Northern Powergrid's business plan as it sets the context for our members' work up to 2023. We believe that the dialogue has been open and constructive as our passion to improve the service to customers is tempered by the need for adequate resources and for clear focus on how we meet the real demands of other stakeholders.
5. In these circumstances, we believe that the business plan is sound and meets the reasonable expectations of other stakeholders. We hope that it can be implemented quickly: it forms a firm foundation for the hard work needed to maintain and improve customer service.
6. We believe that Northern Powergrid must ensure that it pays competitive salaries that reward staff for effective performance and efficiency if it is to operate efficiently and secure a cost-effective balance between the use of directly-employed staff and contractors. High quality training and excellent health and safety management are vital parts of an employment package required to meet the six primary outputs identified in Ofgem's Overview of the Strategy decision for the RIIO-ED1 electricity distribution price control document published in March 2013.¹

¹ Ofgem document 26/13 that identified the six primary outputs as Safety, Environment, Customer Satisfaction, Connections, Social Obligations, Reliability and Availability

7. Northern Powergrid has committed to employ an additional 100 technical and craft staff during each year of the price control. This target has been set after an unprecedented review of staff requirements both within the Company and at national level through the Skills Academy involving contractors and other stakeholders such as Prospect. Up to 2010, constraints on the funding of training restricted recruitment, especially that of highly trained and flexible engineers, which has resulted in severe skills shortages and a distorted age structure in electricity distribution with a substantial proportion of staff due to retire over the next decade. Consequently, the cost of contractors has soared in response to demand and without significant recruitment and training, there is a high risk that long-term costs will increase by substantially more than the rate of inflation.
8. In addition to recruitment, the increased technical sophistication of distribution systems to meet environmental targets and to satisfy consumer demand requires the up-skilling of existing staff. For example, obtaining the full benefit to consumers of the development of smart metering and the use of information captured by smart meters to create smart grids is dependent upon improving the skills of staff whilst retaining a flexible and professional attitude to work. We believe that this has been achieved in DPCR5 (Distribution Price Control Review 5) and believe that the business plans enable us to work with Northern Powergrid to develop and apply the skills necessary for a modern smart network.
9. Health and Safety is vital to Prospect's work: we believe that ensuring that we make every effort to ensure that staff return home after a day's work without incurring injury or disease is a hallmark of a civilised society. In a high risk environment like electricity distribution, constant vigilance and prompt action is key to maintaining and improving high safety standards, both for workers on the system and for the general public. Whilst in the long-term high safety standards reduce costs and improve customer service, in the past Ofgem have declined to include the cost of safety initiatives in their cost base: we believe that recognising the value of safety is a major advance and that the current business plan enables Northern Powergrid to manage safety effectively and maintain its position as a leader in safety across the sector. Over the past ten years, the Company has worked hard with the unions and the HSE to deliver real improvements in safety to meet the standards of management and operational performance required for compliance with UK health and safety legislation.

Overall Quality of the business plan

10. Whilst the plans set out demanding improvements in performance with a declining income from customers, on balance we believe that the plans are well-argued and reflect what the company can deliver with co-operation from staff and other stakeholders. However the experience of DPCR 5 demonstrates that Northern Powergrid can meet demanding business plans and that the IIS (Interruptions Incentive Scheme) provides an effective mechanism for promoting cost-efficient productivity improvements that benefit consumers.
11. The information provided on the plan is extensive and provides us with the feedback we need to inform our negotiation and consultation with Northern Pow4ergrid over the change in staff conditions and improvements in staff engagement required to meet the objectives of the plan. Over the past eight years, we have developed an effective system of employee relations that is focused on the key priorities of the business plan and the changes in skills, practice and attitude required to maintain and to improve an already high standard of customer service. We believe that this collaborative and problem-solving approach to employee relations has benefited staff and the owners of the business: most importantly it has enabled us to make better progress on improving the quality and cost of the service to customers.

12. The plan is stretching and requires further growth in productivity with stringent cost control at a time when the network is changing with increased use of distributed generation, predominantly wind, and the greater use of smart meters. The reduction in regulatory risk demonstrated by a decision by Ofgem to fast-track the proposals by reflecting the quality of the proposals would reduce the cost of capital and thus benefit consumers.

Stakeholder engagement

13. We have long-established and highly productive arrangements for staff engagement that operate well at both a formal and informal level. Due to the development of effective employee engagement and regular discussion about the goals of the business plan, we believe that we got good-quality feedback on progress against the plan and the priority areas for response. The plan builds on the good working relationship between the Company and its staff that allows us to deal with complex and difficult issues that affect key areas of performance: for example, during the current price review, we have made significant progress on improving standby that has a direct benefit to consumers by improving restoration performance. We are comfortable that the plan meets our needs for information about Northern Powergrid's future strategy and that we have the mechanism for developing that knowledge and acting upon it.
14. To the best of our knowledge, we believe that the plan contains sufficient detail for other stakeholders to understand the Company's strategy to provide an efficient and cost-effective electricity distribution service that is key to the competitiveness of Yorkshire and the North East. We believe that the plans make an appropriate balance between the needs of current and future consumers by making significant investment in the network to meet future needs and by maintaining infrastructure promptly: in previous price reviews we believe that Ofgem has encouraged the deferral of investment to maintain and improve technical performance thus transferring costs to future consumers. Given the drive towards a low-carbon economy, it is important that investment does occur over RIIO-ED1 to ensure that Great Britain has the active network required to benefit from technological change needed to reduce the carbon intensity of electricity.

Expenditure proposals

15. Given the increasing costs of materials and skills shortages, we believe that the expenditure proposals are based on a significant increase in productivity. The expenditure proposals to achieve the defined outputs are stretching: this requires our members to continue to improve productivity if they are to see their income maintained, let alone improved so the proposals provide a powerful incentive for the Company's staff to continue to be engaged in improving efficiency. We believe that the plans are well-justified and reflect the deep technical and commercial expertise of Northern Powergrid's professional staff.
16. Whilst initiatives such as the Low Carbon Networks Fund and other types of innovation offer greater financial efficiency and we welcome engineering solutions that make best use of our members' professional expertise, it is important to recognise that these initiatives to reduce the carbon intensity of electricity are expensive. Considerable innovation is required between now and 2023, inevitably some of this will not be optimal for the network as currently configured. Thus Ofgem needs to be realistic about the efficiency gains of new technology during ED1 as the benefits of this innovation are more likely to be realised in later price control periods. On balance we believe that the proposals are optimistic about the benefits of new technology: although we are happy to receive this confirmation of the Company's faith in the ability of its engineers and other professional staff to adapt to change, Ofgem should not assume that the productivity gains before 2023 from this innovation will be simple and easy.

Financial Proposals

17. The price controls requires financial proposals to be proportionate, only interfering with the efficient management of the business where there are clear targeted benefits for the public. Northern Powergrid, and its customers, has benefited considerably from a committed long-term owner who places a high value on developing the business. The proposals are based on a realistic assessment of the cost of both debt and equity in an environment where significant investment in other large-scale infrastructure projects in other sectors is needed.
18. The proposals are complex as regulation must balance a range of interests and deals with a high level of uncertainty as technology and Government policy develop. Northern Powergrid's owners are accepting a high level of financial risk under this plan and the fast-track process is key to reassuring investors that the level of regulatory risk has been minimised and that the business is free to manage its risks. Financial stability is important to us as affordability is a key determinant of salary increases so moves that unintentionally increase the volatility of Northern Powergrid's income are unwelcome

Uncertainty and risk

19. Given the short-term nature of Government energy policy, the plan makes sufficient regard for uncertainty and strikes an appropriate balance between an unduly conservative approach that constraints the application of low-carbon technology and a highly permissive approach that wastes consumer money. Whilst the nature of innovation involves some investment in redundant capacity, the processes designed to share knowledge across the sector should minimise such investment to a level where innovation is not stifled. Whilst the IIS is demanding and punishes dips in restoration performance, we believe that the reliability of electricity supply is the single largest factor behind consumer satisfaction if costs remain stable so the use of such incentives is in the consumers' interests. Therefore we believe that the business plan makes sound proposals for managing risk and the ability to reopen the price control in 2018 if there is significant material change and the existing review processes provides an appropriate balance of risk between the business and its customers.
20. Pensions are a key part of the employment package: in an environment where skills are complex and take a long time to develop then pensions provide a powerful incentive for staff retention. We have developed a reasonable defined contributions pension scheme for staff appointed after privatisation that matches market practice for highly skilled professional engineers and this is a key part of an employment package that is cost-effective and ensures that turnover is reasonable. Higher levels of turnover would increase costs to consumers and pose a greater risk to customer service as there is already an extensive training programme in place to meet existing recruitment needs and ensure that knowledge is developed and transferred between staff effectively. We believe that Ofgem should not intervene in salary setting as this is clear matter to be managed by the employer: intervention in pensions is only justified when there is clear evidence that this is proportionate regulation targeted at a key issue with a significant impact on consumers.
21. We believe that the proposals in place to deal with historic pensions deficits stem from the provisions placed in the Electricity Act 1989 to meet the objectives of Government policy at the time: we are concerned lest the review of pension deficits create a perverse incentive to undermine the protection of pensions by placing other penalties on staff in the Electricity Supply Pension Scheme (ESPS). We believe that as the pensions guarantees were the will of Parliament that Ofgem should not act in a manner that undermines that guarantee.

22. Creating the impression that Ofgem will intervene in remuneration creates a false impression that Government seeks the right to overrule private-sector employers. Given the severe skill shortages in the electricity sector and the difficulties in attracting individuals with engineering and associated skills into the sector, we believe that creating regulatory incentives to constrain the employment package of ESPS members would deter highly-skilled individuals from joining the industry by creating an impression that regulation forces creative accountancy that damages their long-term career prospects and artificially reduces their remuneration. This would increase salaries and thus costs to the detriment of consumers. Therefore we believe that future reviews of pension liabilities should recognise that these historic liabilities are the result of legislation and are substantially linked to staff who have retired from the sector and the proportion of ESPS members remaining in active employment is reducing quickly over the life of the price control.
23. We see the development of staff skills and the development of staff engagement as major protection against an uncertain future by equipping staff with the rounded skills and flexible attitude required to adapt to a variety of future scenarios. As set out in paragraph 7 of this submission, we see continued support for training as being in the interests of all stakeholders to ensure that the service is provided to consumers at the high quality required and at reasonable cost.

Conclusion

24. The regulation of DNOs conforms to the five principles of regulation identified by the Better Regulation Task Force in 1997 and enshrined in the Legislative and Regulatory Reform Act 2006 as follows:
- Proportionality;
 - Accountability;
 - Consistency
 - Transparency; and
 - Targeted
25. We believe that the business plan submitted by Northern Powergrid is robust and well-justified, meeting the five core criteria set out in the March 2013 strategy overview document. Given the provisions put in place to review the outputs and the continued incentives and penalty structure, the plan addresses the legitimate concerns of consumers and other stakeholders and targets those issues that have the greatest impact on performance and customer satisfaction.
26. The business plan has evolved with the input of major stakeholders in the region and has been adjusted to meet the concerns of consumers providing a higher level of accountability than in previous price reviews. Whilst this provides a higher level of challenge to the work of our members, we feel that this feedback provides more targeted approach to the twin goals of price control and innovation. Also this level of consumer involvement in the price control improves the transparency of regulation by engaging key stakeholders in the key debates about the future of the network as electricity distribution undergoes a fundamental change to an active distribution system. In this manner, RIIO conforms to the five principles of regulation in practice as well as in theory.
27. In these circumstances, we believe that fast-tracking the Northern Powergrid is a proportionate and consistent response that would benefit consumers and reduce the cost of regulation. More importantly we believe that as stakeholders ourselves, fast-tracking would remove uncertainty and give us more time to focus on working with Northern Powergrid to provide an efficient and innovative service to the consumers of Yorkshire and the North East.