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Dear James

Consultation on Severe Weather Guaranteed Standards

Thank you for your letter of 31 March 2014 seeking views on Ofgem's suggested amendments to the Guaranteed Standards of Performance relating to supply interruption duration during periods of severe weather.

In this consultation Ofgem makes two proposals:

1. Amending the 2010 Guaranteed Standards of Performance by placing the onus on companies to make automatic payments to customers for all standards covering power loss.
2. Increasing payments to customers for power loss following severe weather events. Ofgem proposes doubling the levels already indicated for RIIO-ED1, from £35 to £70, believing that this may strike an appropriate balance between reflecting the issues raised by the December 2013 storms and the underlying principle behind Guaranteed Standards of Performance being an "inconvenience" payment and not consequential loss. Such a doubling would apply to both the initial payment and subsequent payments. The cap per customer per event would also increase to £700.

In considering our response to these proposals we have considered this from the perspective of our customers and the effects on the Distribution Network Operator companies.

For customers

We agree that companies should make higher payments under severe weather conditions than was proposed in Ofgem's RIIO-ED1 strategy document. This is the right thing for customers whose inconvenience is the same whether a protracted outage happens in 'normal' conditions or in severe weather conditions. We also believe that Ofgem should consider introducing a payment to customers after 12 hours of, say, £35 to recognise the inconvenience of being off supply for that period of time.

We agree that payments should be paid automatically wherever the company has the data to facilitate this.

For companies

The effect of Ofgem's proposition on companies is that their risk profiles are increased, but no recognition is given of this in the consultation.

Payments under guaranteed standards are not subject to the totex efficiency sharing factor so the whole amount is borne by the company. The only protection companies have is a downside cap in licence condition CRC2D on the total amount paid, currently £12.3m in any one year (2012-13 prices) for Electricity North West. This is a significant amount of money to have to pay out for events that cannot be prevented. Doubling the amount companies have to pay doubles companies' risk of being exposed to that amount.

We agree with Ofgem's principle that payments should represent an "inconvenience" payment and not consequential loss. Any move towards requiring companies to make payments relating to consequential loss would significantly change companies' risk profiles away from that envisaged at privatisation.

For customers and companies

Ofgem's consultation retains the differentiation between category 1, 2 and 3 events with different payment timings and levels of payments. This differentiation was introduced to reduce risk exposure for companies for big events, which is important but which comes with its disadvantages:

- For customers, they will not understand how bad the storm is that causes them to be off supply, and waiting another day before being eligible for compensation because a company had one extra fault and passed an additional threshold can be a cause of additional dissatisfaction because customer impact for individual customers will be no different.
- For companies, firstly if an event hit the category 3 threshold (for Electricity North West just over quarter of million customers) customers could be off supply for more than 48 hours and receive no compensation, which could create a political and media issue for the industry.
- And secondly for companies, it can mean that companies may not know how much they need to pay out or when payments are due from until they have detailed fault data. This can make communicating with customers and confirming what payments they will receive difficult – particularly when faults occur over a protracted period.

Electricity North West recommendation

Based on the factors set out above, we believe that this is an ideal opportunity to simplify the Guaranteed Standards relating to severe weather. We recommend the following approach be taken to establishing the RIIO-ED1 approach.

1. We propose that there is only one exceptional event threshold applicable during severe weather, which we suggest is aligned to the current IIS exemption threshold.
2. We agree that companies should make higher payments under severe weather conditions than was proposed in Ofgem's strategy document for RIIO-ED1. We also agree that any subsequent payments should also be increased and that the cap of the maximum amount payable to an individual customer should be increased to £700.
3. We propose that the amount payable to a customer should not change depending on the severity of the severe weather. We support a standard £35 payment after 12 hours and £70 payment after 24 hours under all severe weather conditions.
4. We support the proposal to make payments to customers automatically wherever the DNO has the necessary information to facilitate this.

5. To recognise that this increases risk on DNOs, we propose that if IIS exemption levels are reached then companies should be able claw back the difference between what they have paid under the revised standards and the amount that would have expected to be paid based on approach set out in Ofgem's RIIO-ED1 strategy document. This could be achieved by introducing a new mechanism into CRC2D that would be similar to, but admittedly more complicated than, the mechanism already included in the draft RIIO-ED1 licence for one-off events. In this way customers always get a payment regardless of the severity of the event but a company's risk profile is no different to RIIO-ED1 strategy expectations. Regardless of whether Ofgem agrees that we should simplify the mechanism to just one category of severe weather event and introduce payments after 12 hours, a mechanism such as this is essential to ensure that companies' risk profiles remain unchanged from that envisaged in Ofgem's strategy document and assumed in companies' cost of equity proposals.

We recognise that this is an alternative proposal, building on the suggestions in the consultation letter, and would be willing to work with you to draft the required licence mechanism.

I trust that you find our response helpful and please do not hesitate to contact me if you have any questions relating to it.

Yours sincerely



Sarah Walls
Head of Economic Regulation