

**By E-mail**

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Dear Chris,

**Consultation on Close out methodologies for the DPCR5 Price Control**

We welcome the opportunity to comment on your close out methodologies consultation for the DPCR5 Price Control dated 29<sup>th</sup> September 2015. As requested we have structured our response based around the questions set out in Appendix 1 of the consultation.

**Network Output Measures**

**Do you agree with the principles for the NOMs assessment?**

We support the six principles detailed for the assessment of NOMs. The inclusion of output measures within the price control is essential to ensuring DNOs deliver benefits for customers. However this needs to be achieved through a flexible mechanism which encourages DNOs to innovate, respond to new information and effectively address risks as they arise or change during the regulatory period.

The principles provide a strong basis to establish the methodologies for assessing output measures and allow DNOs to demonstrate how they have delivered output measures to the benefit of customers.

**Do you agree with our approach to assessing performance on Health Indices?**

We agree with the three stage approach to assessing Health Index output delivery performance. The performance assessment submission is the fundamental starting point for the assessment. This places the emphasis on DNOs to explain what they have delivered during DPCR5, how it varies from the agreed output measures and why the changes have occurred.

For the quantitative assessment use of the risk point methodology, developed during DPCR5, provides a common basis for changes in delivered outputs to be explained. Ofgem have outlined the methodology that will be used to undertake a sensitivity analysis of the unit costs and Health Index weightings. This is important to understand how outputs may vary and to highlight areas of focus for the qualitative

assessment. The baseline weightings were discussed and utilised during DPCR5 to report output progress and the DNOs have continued to use these in monitoring and assessing output delivery progress. It is important that these are retained and used as the main measure of health index outputs.

Ofgem have highlighted the key criteria it will review while undertaking the qualitative assessment. The first three of these focus on review of the DNOs explanation of what they have delivered, how it varies from the agreed outputs and the impact of any material changes on the delivered outputs. The fourth and sixth look at the absolute position in the Health Index categories and the fifth checks the quality of the Health Index returns against other data returns during DPCR5.

We are supportive of these criteria, with particular focus on the first three. It is important that Ofgem is satisfied that the DNOs explanations of their delivery and changes which have impacted that delivery are justified, appropriate and in the interests of customers. It is also appropriate that DNOs can explain the absolute position in Health Index categories and justify where this is poorer than forecast. Whilst the check against other data returns is useful it would only be an important factor if there are significant variances which cannot be justified by the DNO.

Overall we agree with the approach to assessing performance on Health Index outputs and believe it provides an appropriate balance between quantitative and qualitative measurement, whilst supporting the principles for outputs detailed within the DPCR5 Final Proposals.

**Which of the two approaches to valuing the Health Indices outputs gap do you consider to be more appropriate?**

We support the first option for valuing the Health Indices outputs gap as it is consistent with the principles outlined within the NADPR RIGs and provides an appropriate penalty for non-delivery of outputs.

We believe that the second option is flawed as it calculates a £ per risk point value based on a DNO's delivery during DPCR5. If a DNO has changed its plans from the agreed outputs to focus on undertaking low cost risk point movements during DPCR5 and deferred high cost movements it will get a relatively low £ per risk point value which doesn't align with the agreed outputs. This would result in a lighter penalty being applied and disadvantage customers.

The second option could be improved by calculating a £ per risk point based on allowances rather than delivery. This would allow the value of the outputs gap to be calculated in similar way to the Load Index approach. The risk point delta for each category could be converted to a value of work and then multiplied by the allowed DPCR5 unit cost to provide the allowance value. This would then be divided by the risk point delta to provide the £ per risk point for the agreed outputs.

**Do you agree with our approach to assessing performance on Load Indices and valuing any associated outputs gap?**

Overall we support the proposal to assess performance based on a qualitative assessment of actual vs agreed Load Index profile based on risk points with any output gap valued using £ per risk point. We believe the proposed approach provides an appropriate balance between quantitative and qualitative assessment.

We note that page 56 of Appendix 2 states that; *"If the DNO has delivered a worse load profile than agreed at DPCR5 or the number of risk points is higher, the DNO should provide a justification of:"* Our response makes the assumption that "load profile" refers to "Load Index profile".

**Do you agree with our approach to assessing fault rate performance?**

In principle we support the approach to assessing fault rate. Fault rate is a useful secondary measure where Health index data is not available. However they are a lagging indicator and do not provide a direct correlation with expenditure. This means that a qualitative approach discussing trends is the most appropriate treatment. We note the reference to the terms 'Risk Point Methodology' and 'Risk Point Analysis' in paragraph 2.39. These should not apply to fault rate outputs and believe they are a typographical error.

**Do you agree with our proposal not to make any financial adjustments associated with fault rate performance?**

We agree with Ofgem's proposal not to apply financial adjustments as defined in Table 2.1. This is consistent with the basis of the DPCR5 Final Determination when Ofgem recognised that these measures may be driven by factors outside of the DNOs control, for example weather patterns.

It is also our view that an assessment of fault rates for DNOs should consider benefits delivered for customers across the portfolio of assets reviewed rather than looking at individual categories, and should consider these in the context of the volumes of asset renewal anticipated by the DPCR5 Final Determination.

**Do you agree with the changes we have made to the assessment approach from DPCR5 FPs and the NADPR RIGs?**

We agree with the changes made to the approach from the DPCR5 FPs and the NDAPR RIGs. The Heath Index metric was intended as a good measure to demonstrate the condition of asset classes. There was also a desire to move towards a higher level metric which also provided an understanding of risk across asset categories. Introducing a quantitative assessment based on the risk points methodology moves towards this as it provides a basis for DNOs to explain their changes and aids understanding of the overall risk position for Health Indices.

We are supportive of the application of a materiality threshold based on risk points rather than the 'significant and material' terminology included in the Final Proposals. This is possible with the use of the risk point methodology and provides transparency for DNOs and stakeholders in understanding output delivery and any penalties.

We agree with the proposals for material changes and agree that this is an improvement on what was proposed at the start of DPCR5. The impact of material changes is embedded within the current Health Index approaches for each DNO. It would require significant effort to unpick these so as to update the agreed outputs for the material changes. DNOs should be able to detail and explain their material changes and Ofgem should take a view on whether these are appropriate or not.

**Load Related Reopener**

**Do you agree with the principles for the load-related reopener assessment?**

We generally support the principles detailed for the Load Related Reopener but there are outstanding questions regarding the level of supporting information that will be needed to complete the assessment. The inclusion of output measures within the price control is essential to ensuring that DNOs deliver benefits for customers. However this needs to be achieved through a flexible mechanism which

encourages DNOs to innovate; respond to new information and effectively address risks as they arise or change during the regulatory period.

It is important that Ofgem provides comprehensive guidance to the DNO of the level of information to be provided if a reopener has been triggered, and that this information is proportionate. It is our view that the DNOs should be given the opportunity to comment on proposed guidance before a reopener is triggered.

In Principle 9 (*We will consider any inefficiencies due to projects being carried out where they were no longer needed or for an inefficient level of costs*) it should be noted that economic swings are complex to predict and that the decision to abandon a project versus delay or to part complete is not simple. It is important that any assessments also consider if a reasonable decision has been made based on the information available at that time.

It is also our view that DNOs should not be adversely disadvantaged by a reopener providing expenditure is proved to be efficient i.e. 70% efficient expenditure is far more preferable than 80% inefficient expenditure.

The principles provide a strong basis to establish the methodologies for assessing output measures and to allow DNOs to demonstrate how they have delivered output measures to the benefit of customers.

#### **Do you agree with our approach to assessing expenditure on low volume high cost (LVHC) connections?**

The proposed quantitative and qualitative assessment based on change in volume and proportion of cost that has been recovered upfront through connection charges seems reasonable providing the qualitative assessment ensures DNOs are not unfairly disadvantaged.

Due to the individual nature of LVHC connections benchmarking using the industry mean may unreasonably disadvantage some DNOs due to individual connection specifics that have appropriately benefited customers. As a consequence we are supportive of Ofgem's approach providing qualitative adjustments are made where appropriate.

#### **Do you agree with our approach to assessing expenditure on general reinforcement?**

We are supportive of Ofgem's approach to assessing expenditure on general reinforcement. It is our view that this is a complex assessment that will vary due to DNO specifics, including local economic conditions and existing network characteristics. Therefore DNOs should be given the opportunity to review and feedback on the draft output of the assessment before adjustments are made.

We would welcome to opportunity to work with Ofgem to develop this assessment.

#### **Do you agree with our approach to assessing avoided reinforcement?**

We are supportive of Ofgem's qualitative approach to assessing avoided reinforcement based on the strength and justification of the information provided and the use of cost benefit analysis to demonstrate innovative techniques deliver benefits to customers.

## High Value Projects

### Do you agree with the principles and general approach set out in this chapter?

We agree with the principles and support the approach to the assessment of high value projects. As HVPs vary in terms of project type and outputs the assessment needs to be tailored towards the appropriate type.

### Do you agree with the changes we have made to the assessment approach from DPCR5 FPs?

We agree with the changes made to the approach from the DPCR5 FPs and the NDAPR RIGs. We support the approach to bespoke outputs assessment using existing methodologies as appropriate and the development of additional methodologies.

### Do you have any suggestions on how we can assess outputs under the individual project categories set out in this document?

For BT21CN projects the solution is dependent on a wide range of factors including; available technologies, existing fixed infrastructure and existing infrastructure services. We believe that for BT21CN projects an assessment of the outputs based on the circuits completed taking into consideration the solution applied and efficiency is the most appropriate. While cross DNO cost benchmarking is possible in this area, care should be taken in order to ensure that the benchmarking is on a like for like basis and reflects previous Ofgem guidance regarding DPCR5 BT21CN projects.

## Traffic Management Act

### Do you agree with our proposed methodology for adjusting DNOs' allowances to account for permitting costs?

We agree with the proposed methodology and principle for adjusting DNO's allowances to account for permitting costs. Collation of such data may prove challenging but the rationale is understood (E.g. collation of data to adhere with permit costs over and above adhering to NRSWA).

### Do you agree with our proposal to settle the TMA reopener mechanism early as part of the 2016 annual iteration?

We support the proposal to settle the TMA reopener as part of the 2016 annual iteration methodology.

If you have any queries on this response please do not hesitate to contact myself on the number above.

Yours sincerely,



**Jim McOmish**  
**Head of Distribution Network**

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