

By E-mail

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Date

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Contact / Extension

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Dear Grant,

DPCR5 Close out: Statutory Consultation on changes to the RIIO-ED1 Financial Handbook

We welcome the opportunity to respond to Ofgem's DPCR5 Close out: Statutory consultation on changes to the RIIO-ED1 Financial Handbook published on the 20th June 2016. Overall we support the majority of the proposed methodologies and believe the drafting reflects the significant effort invested by all parties in the working group to produce robust approaches for each area.

The final drafting incorporates many of the revisions suggested by ourselves and the other respondents to last month's informal consultation. The informal consultation provided a useful step in the process as it allowed areas of concern to be highlighted, discussed and reviewed prior to the statutory consultation.

The appendix to this letter sets out some detailed comments on the drafting whilst this letter sets out our views on some points of principle.

NOMs – Fault rate measure and Overall Assessment

Overall we do not believe that the application of penalties to fault rate performance provides a direct link to investment activity during DPCR5. However, we believe that Ofgem have responded to these concerns and have developed an approach which reviews actual performance against forecasts, on a like for like basis, and provides DNOs with the opportunity to provide justification to explain the actual performance. This explanation can include discussion of the costs and benefits of proactive investment versus faults. This allows the methodology to account for the relative economics of the impact of faults on customers and DNOs via the Quality of Supply mechanisms and the Efficiency Incentive Rates (for both fault costs and asset replacement costs) in order to ensure that any penalties are proportionate and balanced. Only in cases where it is viewed that the justification is insufficient will it be determined that there is an outputs gap for the fault rate component of NOMs.

In addition the proposed methodologies present NOMs as an overall assessment based on a suite of measures covering Health Index, Load Index and fault rate, consistent with DPCR5 final proposals. Therefore performance against each component of the NOMs will be taken into account when determining the overall value of any outputs gap. This approach provides flexibility for DNOs to

demonstrate how they have delivered a suite of outputs consistent with the DPCR5 final proposals through effective asset management over DPCR5.

The revised drafting to assessing the NOMs Network Outputs Gap makes clear how the different components will be combined and that the Authority will take into consideration the information from each component when determining the overall gap. We welcome this clarity and believe it presents a concise approach which, when combined with the proposed consultations, will provide transparency to this step of the process. How the Authority has calculated the NOMs Network Outputs Gap will need to be clearly presented in the public consultation process to ensure that a fair and transparent process is evident to all.

In responding to the informal consultation we supported the use of a higher materiality threshold for the fault rate component of the NOMs than for Health Index and Load Index. However, we proposed that the threshold should be 18%, based on our analysis, rather than the suggested 10%. We note that threshold remains at 10% and that Ofgem believe this 'properly accounts for the additional uncertainty associated with factors such as annual weather fluctuations, third party damage, overloading, bird strikes and defects'. We recognise the arguments presented by Ofgem and can see that a threshold of 10% does go some way to mitigate the external factors which can influence fault rates. As the methodology allows for DNOs to explain variations in fault rates beyond the threshold and for the Authority to review these and agree to them as an acceptable explanation without the application of penalties we can accept 10% as the threshold.

Treatment of Real Price Effects


The methodologies for the re-openers for Load Related Expenditure and for High Value Projects propose that expenditure is adjusted for the variation in Real Price Effects (RPE). We support this approach as the DPCR5 Final Proposals clearly allocated the risk of variation in RPEs to the DNOs. Therefore the impact of this variation needs to be adjusted for in assessing the two re-openers.

Conclusion

We believe that the proposed methodologies will also allow DNOs to demonstrate to stakeholders the significant customer benefits that have been delivered in this period. The methodologies are the output of significant effort by Ofgem and all the working group members over the past year.

If you have any queries on this response or any further questions, please do not hesitate to contact me.

Yours sincerely,



Jim McOmish

Head of Distribution Network

SP Energy Networks

Attachments: Detailed comments on drafting

Question 1: Do you have any views on the proposed changes to the Financial Handbook? The draft methodologies are found in Supplementary Annex 1.

We have set out some detail changes to the handbook and our specific areas of concern are highlighted in the sections below.

Chapter 15

Para 15.125 – Amend ‘that was incurred as part of DPCR5 HVP’ to ‘that was incurred as part of a DPCR5 HVP’.

Para 15.133 – Text references paragraph 0, this should be changed to paragraph 15.130.

Para 15.135 – Text references paragraph 15.10; this should be changed to paragraph 15.11 as this is where the Authority’s Preliminary View will be provided.

Para 15.139 – Delete reference to footnote 4 in sub paragraph (e) as this has been removed.

Para 15.143 – Text references paragraph 15.10; this should be changed to paragraph 15.11 as this is where the Authority’s Preliminary View will be provided.

Para 15.189 - Amend ‘This subsection sets out how we will...’ to ‘This subsection sets out how the Authority will...’

Para 15.201 – line 4 ‘amount’ should be ‘Amount’

Para 15.204 – sub para (a) insert Expenditure between baseline and allowance

Para 15.209 – sub para (e) is inconsistent with para 15.139 (g)

Para 15.221 – sub para (a) the reference 0 should be to para 15.202

Para 15.222 – reference to step (viii) should be to step (vii)

Annex A1 NOMS Failure to Deliver Outputs

Overview

Para 1.5 – Step 3 refers to determining whether a NOMs Network Outputs Gap has arisen. This is also referred to in step 4. Therefore we believe that the terminology in this step is incorrect. Step 3 reviews whether or not the agreed, or the adjusted, outputs have been delivered for each component of the NOMs. Suggest that step 3 is amended to:

‘Step 3: Determination of whether the agreed, or the adjusted, outputs have been delivered for each of the output measures in paragraph 1.2 above (see paragraph 1.14 to paragraph 1.15)’

Para 1.6 – Text references paragraph 1.4, this should be changed to paragraph 1.5 as this is where steps 1 to 3 are defined.

Para 1.7 – The current drafting infers that if projects were included in the Agreed Network outputs they will be included in the NOMs assessment. This could lead to double counting as they will be assessed twice, in NOMs and in HVP outputs.

Para 1.13 – amend the second bullet to ‘assessing delivery against the Authority’s view of the Adjusted Network Outputs (Step 2B).

Para 1.20 – amend the end of the sentence to read ‘...as specified in paragraph 1.72 to paragraph 1.74.’

Health Indices

Para 1.34 (ii) – amend the end of the sentence to read ‘...does not meet the test set out in paragraph 1.21 and an outputs gap has arisen for the HI component of the NOMs.’

Load Indices

Para 1.45 – Text references paragraph 2.6 of Annex E, this should be changed to paragraph 3.5 of Annex E as this is where the principles for rebasing LI Band Profiles is described.

Para 1.49 (ii) – Amend ‘the result from paragraph 1.45 does not meets’ to ‘the result from paragraph 1.45 does not meet’.

NOMs Network Outputs Gap

Para 1.75 – this issue links back to our previous comment on HVPs (para 1.7). We believe that the clearest way of treating HVPs and avoiding double counting is to exclude HVPs from the agreed and delivered NOMs outputs and assessing them separately as part of HVPs. Treating HVPs in this way would mean that the drafting in this paragraph is not required.

Annex A2 NOMS Risk Point Methodologies

Health Index

Para 1.6 – Amend ‘Weightings are calculated as described in (A)’ to ‘Weightings for each case are calculated as described in (A)’

Para 1.6 – Under unit cost (B) the two paragraphs describing how weightings are calculated can be deleted as the approach is covered by the statement before, and the descriptions in, unit cost (A).

Load Index

Para 1.7 – Text references paragraph 1.40(i), this should be changed to paragraph 1.40(iv).

Para 1.10 – Amend ‘The Authority will conduct a detailed Performance Assessment...’ to ‘The Authority will conduct a Performance Assessment...’ in line with paragraph 15.9.

Annex C2 HVP Outputs Review Methodology

Para 1.9 – Amend the start of the sentence to read ‘The licensee will be required to submit a Performance Assessment Submission...’