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To electricity distribution
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parties

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Decision to approve modifications to the Common Network Asset Indices Methodology v1.1

On 3 February 2017, the distribution network operators (DNOs) consulted upon modifications to the Common Network Asset Indices Methodology ('Common Methodology')¹. On 20 April 2017, the DNOs submitted the revised Common Methodology to Ofgem for approval. We have decided to approve these changes and this letter explains the reasons for our decision.

1. Background

As part of the RII0-ED1 price control review, DNOs provided forecasts of their asset health and criticality positions 'with intervention' and 'without intervention'. We used these to create secondary deliverable targets², setting out the required improvements in asset health, criticality and monetised risk.

SLC 51 of the Licence requires the DNOs to have a Common Methodology for asset health, criticality and monetised risk. The DNOs have worked together to develop the Common Methodology and following a series of consultations, we approved v1.0 on 21 October 2016³.

During the rebasing of the Network Asset Secondary Deliverables (NASD) targets, the DNOs identified changes to the Common Methodology v1.0 to address the overstatement of the perceived risk for specific asset categories. The DNOs consulted on the Common Methodology v1.1 on the Energy Networks Association (ENA) website from 3 February 2017 to 3 March 2017⁴. One respondent considered that they were unable to properly respond on the basis that there was insufficient detail provided. Therefore, the DNOs published additional information on the ENA website to allow for further representations.

A single response was received to this supplementary consultation and the DNOs have submitted their report under SLC 51.25 on 20 April 2017. Both reports and the responses are published alongside this approval letter.

¹ pursuant to Standard Licence Condition ('SLC') 51.24 of the Electricity Distribution Licence (the 'Licence')

² Secondary Deliverables sit under the Reliability and Safety Outputs of the RII0 framework. They enable us to monitor companies' performance and are leading indicators to ensure long-term delivery and value for money.

³ <https://www.ofgem.gov.uk/publications-and-updates/decision-distribution-network-operators-common-network-asset-indices-methodology>

⁴ <http://www.energynetworks.org/news/publications/consultations-and-responses/>

2. Common Methodology requirements

SLC 51.11 contains the key objectives for the Common Methodology. It should enable:

- '(a) the comparative analysis of network asset performance between DNOs over time;
- (b) the assessment of the licensee's performance against the Network Asset Secondary Deliverables; and
- (c) the communication of information affecting the Network Asset Secondary Deliverables between the DNO, Ofgem and, as appropriate, other interested parties in a transparent manner.'

The Common Methodology should enable the evaluation of risk 'trade-offs' between asset categories and the delivery of a risk profile within a single asset category that is different to the target profile, to clearly define the level of under- or over-delivery achieved. It should also facilitate the increase in the scope of assets covered by the framework to eventually include all asset categories in the asset register.

We set out criteria by which to assess the Common Methodology, and shared these with the DNOs through the Common Framework Working Group in December 2014. We have used these to guide our consideration of whether the revised methodology meets the Licence requirements.

3. Responses

A single response was received from British Gas to the DNO's initial consultation and this is published alongside this approval letter.

British Gas raised two points:

1. it made a comment on the ability of consultees to fully understand the background and logic of the proposed changes based on the information presented, although it also stated that the changes look sensible in isolation; and
2. it stated its opinion that it is inappropriate to adopt the Common Methodology at this time. It considered that the DNOs should be held to the original targets established via their legacy methodologies as part of the RIIO-ED1 price control process.

In order to address the first of these points, the DNOs agreed to publish supplementary information on the reasons for the proposed changes and to allow interested parties an additional appropriate period of time in which to make representations. A single response to the DNOs supplementary consultation was received from the same respondent, British Gas, and this is also published alongside this approval letter.

British Gas raised three key points:

1. the additional information provided as a result of the supplementary consultation has improved the respondent's understanding of the proposed changes and therefore permits it to present an opinion on the changes.
2. it is concerned that the removal of outliers and averaging of data in the calculation of parameters will create systematic over or under estimation of risk relative to individual licensee experience and hence create sub-optimal asset management practices.

3. it continues to emphasise its view that it is inappropriate to adopt the Common Methodology at this time and that the DNOs should be held to the original targets established via their legacy methodologies as part of the RIIO-ED1 price control process.

The additional information published in the supplementary consultation has addressed the first point and the respondent stated that its understanding of the proposals has improved. Our view is that the additional information allowed interested parties to make an informed representation and enhanced the transparency and robustness of the Common Methodology.

For the second point raised on the supplementary consultation, we accept the DNOs response that it is appropriate to use data averages given this was a key principle during the development of the Common Methodology and was subsequently approved. The DNOs also confirm that the outliers excluded are mostly unreliable historical data. Hence, we agree that it is appropriate to remove such outliers to ensure that the parameters used are representative of the industry average.

With regard to the third point, British Gas previously raised this during the original consultation on the Common Methodology. Our decision on 23 October 2015⁵ sets out our response and we are still of the same view given the consultation on the NASD Rebasing⁶.

4. Our decision

We have considered the Common Methodology v1.1 in line with the various criteria outlined above and the responses received during the DNOs consultation and have decided, pursuant to SLC 51.27, not to object to implementation of the proposed modifications. We have decided to approve the Common Methodology in its current version. This approved Methodology is published alongside this letter.

Under SLC 51.26, the licensees may notify the Authority that the implementation of any modifications may require a change to the licensees' Network Asset Indices Methodology, or Network Asset Workbook, or may require a restatement of data previously reported. The licensees have confirmed that they do not propose to submit any such notice to the Authority as the modifications have already been incorporated in their Network Asset Secondary Deliverables Rebasing submission⁷.

Yours faithfully,

Min Zhu
Associate Partner Networks Analysis

⁵ <https://www.ofgem.gov.uk/publications-and-updates/dno-common-network-asset-indices-methodology>

⁶ <https://www.ofgem.gov.uk/publications-and-updates/network-asset-secondary-deliverables-rebasing-consultation>

⁷ <https://www.ofgem.gov.uk/publications-and-updates/network-asset-secondary-deliverables-rebasing-consultation>