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19th April 2017

Ofgem Consultation on Mid-Period Review Parallel Work

Dear James,

Wales & West Utilities is one of eight licensed Gas Distribution Networks (GDN) regulated by Ofgem, we provide gas transportation services in Wales and the South West of England for all major, and most smaller, shippers in the UK. We cover 1/6th of the UK land mass and transport gas to over 2.5 million supply points. We transport gas from the national grid transmission system direct to domestic, commercial and industrial sites.

We welcome the opportunity to respond on the mid-period review parallel work, where we have provided answers to your questions below.

We are broadly supportive of the proposed approaches suggested by Ofgem to the issues identified in this MPR Parallel work.

○ **Chapter 1 – Background and Scope**

Question: Do you agree with the scope of the MPR parallel work?

We support the scope of this MPR parallel work. We think Ofgem has identified some material issues but maintained a sensible balance with regulatory certainty that is important for investors and stakeholders.

○ **Chapter 2 – Output Accountability - When should we consider an output delivered?**

Question: Do you think we are right to focus on the output purpose where there is ambiguity to decide when an output is delivered? If not, please explain why and provide evidence.

We think focus on Output purpose (i.e. achieving the required outcome as set out in the price control) is correct and a key element of RIIO that will promote innovation and efficiencies for customers. It is correct to incentivise networks to deliver Outputs (through ensuring the required outcome is achieved rather than focusing on the method of achievement) at the lowest Totex cost.

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Question: What do you think about our alternative options including focusing on the detailed output specification or output declassification? Will they achieve our purpose? Can you think of any other alternatives?

To focus on detailed Output specification would stifle innovation, constrain new ideas and ultimately lead to potential increased costs and ineffective outcomes for customers. We have not identified alternatives.

○ **National Grid Gas Transmission’s compressors output**

Question: Do you agree with our proposed approach to hold NGGT to account if it complies with the IED requirements? If not, please explain why and provide evidence?

If the Output funded is compliance with the IED and National Grid Gas Transmission has delivered this Output then we do not think any further action is required. Please note that we think there is an error in this question as the recommendation within the consultation is to deem that NGGT has delivered the output utilising innovative options at lower costs to customers.

○ **SP Transmission’s voltage control**

Question: Do you agree with our approach to consider the output delivered if SPT manages voltage across its network efficiently? If not, please explain why and provide evidence?

We agree with the Ofgem approach with regard to SP Transmission’s voltage control as this appears to be a consistent application of the principles applied elsewhere in this consultation. Again, this highlights our support for Ofgem to focus on Output purpose, and the achievement of the required outcomes as opposed to detailed output specification.

○ **Chapter 3 – Price control adjustments – When should we address gaps in the price control**

Question: Do you agree with our proposed approach to delay allowances due to the delivery of the Western HVDC? If not, please explain why and provide evidence?

This is a material cost (£1 billion), we therefore acknowledge why a delay to funding is being considered. The point that we would highlight is one of symmetry. There may be instances where material costs may be required earlier than funding allowances. If a principle is established where late delivery attracts delays in funding, then funding should be made early for material costs that are incurred early.

Question: Do you have any views on how we should delay allowances? Please explain and provide evidence?

Our understanding is that a Direction will be required from Ofgem within an Annual Iteration Process and adjustments will need to be made through the Price Control Financial Model on an NPV neutral basis.

Question: Do you have any view on how we should treat payments and in-kind benefits from suppliers paid to compensate for the delay? Please explain and provide evidence?

If the network is able to demonstrate that the payments made to compensate for the delay are “efficient” and unavoidable, then there is an argument that they should be funded through Totex, just as efficiencies in cost reductions are shared through shipper charges.

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○ **London medium pressure (Gas Distribution)**

Question: Do you agree that we should accept National Grid Gas Distribution's (NGGD) proposal to return £53.9 million? If not, please explain why and provide evidence?

Provided NGGD has been able to provide credible evidence that it has done all it can and exhausted other options to deliver this Output, then this appears to be a sensible solution for customers and the network.

○ **Connections Volume driver (Electricity Transmission)**

Question: Do you agree with our proposed approach not to amend SPT's connections volume driver? If not, please explain why and provide evidence?

We support a symmetrical approach to the application of allowances. The consultation states that there may be an asymmetrical impact on customers as other underspends may not be corrected within this mechanism. If this is the case, we support the Ofgem position.

○ **NTS exit capacity incentive (Gas Distribution)**

Question: Do you agree that we should not make changes to the NTS exit capacity incentive? If not, please explain why and provide evidence?

We agree Ofgem should not make changes to the NTS exit capacity incentive. The incentive does drive gas distribution networks to book efficient levels of exit capacity with the NTS, seek alternative options and hence drive innovation and benefits for customers. We regularly attend the NTS charging forums, engage in the valuable developments and seek to ensure fair, sustainable and transparent costs for our network customers.

However, there are issues with the current pass through arrangements that place an unacceptable level of cash flow risk on gas distribution networks. National Grid Gas Transmission is allowed to change prices in line with its Licence Obligations and UNC duties but gas distribution networks must then wait for a circa 18 month period to recover unfunded increases. There are no caps or collars on the level of charge change to gas distribution networks. There is also a temporary distortion for the market participants where customers connected to the distribution network will not face the NTS increases at the same time as NTS direct connects. This is particularly challenging when there are material changes of double digit percentages on costs that are in excess of £20m per annum for certain gas distribution networks. We have raised this significant issue with Ofgem and industry participants; and will continue to seek better and more sustainable mechanisms through the NTS charging forums.

○ **Gas Distribution Outputs**

○ **Safety repair risk**

Question: Do you agree with our proposed approach to continue to monitor this output for the remainder of RIIO-GD1 and require companies to justify where they fail to meet this output? If not, please explain why and provide evidence?

We support continual monitoring of this Output for RIIO-GD1. We also believe that consideration should be given to reviewing 1 year vs 8 year outputs for RIIO-GD2 as a number of 1 year outputs are heavily impacted by weather so measuring performance over a price control rather than year by year may be more appropriate. We have experienced mild winters so far in RIIO-GD1 so we would support analysis of a winter normalisation factor when setting future targets that are heavily impacted by winter severity.

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○ **Reliability – Loss of supply**

Question: Do you agree that we should change the targets for the loss of supply output for the remainder of RIIO-GD1, continue to monitor performance and require companies to justify where they fail to meet this output? If not, please explain why and provide evidence?

There is evidence that the targets for this Output area are inconsistent between the GDNs. Also, we believe that certain elements for networks should be measured separately to promote comparability – eg loss of supply related to Multiple Occupancy Buildings should be a separate measure due to the different conditions affecting reconnecting their supply.

We would support changing targets but Ofgem must ensure that there are clear, evidenced and transparent mechanisms in place to ensure that any changes are equally challenging for all networks and work to the benefit of customers. We have worked extremely hard within the first four years of RIIO to deliver on our targets to date.

Longer term and into RIIO GD2, this is an area where we can develop our thinking with Ofgem to ensure that the output is one that actually benefits customers. As an example, the existing Output refers to gas on at the emergency control valve (ECV) but customers will be interested in gas available to them at appliance following our works. We will continue to work with Ofgem and the other GDNs in this area.

Attached is a copy of our response to Ofgem's Review of Primary Output Measure - Customer Interruptions in May 2016 as an Appendix to this letter.

○ **Maintaining operational performance**

Question: Do you agree with our proposed approach to make no changes to this output for the remainder of RIIO-GD1, to continue monitoring this output and to require companies to justify where they fail to meet this output? If not, please explain why and provide evidence?

The Maintaining Operation performance Outputs are secondary deliverables and we agree that it is sensible not to change Outputs in this area. We agree the Outputs, and the outcomes achieved, should be monitored and justifications provided by networks for their performance.

○ **SPT Trigger mechanism**

Question: Do you agree with our proposed approach to this trigger mechanism? If not, please explain why and provide evidence?

We agree that the Network Output Measures (NOMs) methodology can be used to incentivise this type of asset investment. We have not been engaged in the discussions of the detailed mechanisms that exist within the Electricity Transmission settlement and therefore we cannot provide any further input on this question.

○ **Electricity Transmission – other Outputs**

Question: Do you agree with our approach to these outputs?

From the evidence provided within the consultation, we support the Ofgem approach to the Outputs. The consultation clearly states that the Outputs have either been delivered, are being delivered or have an existing mechanism to incentive the Output.

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We trust you have found our response to your questions valuable and if you should wish to discuss any aspect of this response do not hesitate to contact me.

Yours sincerely,



Steve Edwards
Director of Regulation and Commercial
Wales & West Utilities

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