

Mark Hogan  
Acting Head of RIIO Electricity Distribution  
Ofgem  
10 South Colonnade  
Canary Wharf  
LONDON  
E14 4PU

1 May 2019

Dear Mark

### **Consultation on the closeout methodologies for RIIO-ED1**

Thank you for the opportunity to respond to the above consultation. This response is on behalf of UK Power Networks' three distribution licence holding companies: Eastern Power Networks plc, London Power Networks plc, and South Eastern Power Networks plc. We are the UK's largest electricity Distribution Network Operator (DNO), dedicated to delivering a safe, secure and sustainable electricity supply to 8.3 million homes and businesses.

The RIIO framework has proven to be successful in driving significant performance improvements in the electricity system and, therefore, benefits to customers through a higher quality of service and lower bills. One of the strengths of the framework is the arrangements for dealing with areas which are uncertain at the time of setting price controls. These uncertainty mechanisms play an important part in managing the risk between customers and DNOs. Therefore, we appreciate the significant work that has gone into developing these eight methodologies over the past 12 months in advance of them being put into action at the end of the current regulatory period. We believe this work has successfully produced methodologies which give effect to the policy set out by Ofgem in the RIIO-ED1 licence for these areas of uncertainty.

The closeout of the DPCR5 price control period showed how these mechanisms can successfully make adjustments in relation to material changes that could not be foreseen or quantified when setting the price control. Building on the hard work and lessons learned from this previous closeout process has led to a strong set of methodologies for closing out the RIIO-ED1 price control. Therefore, we support these methodologies and agree that they will achieve their goal of managing the risk of underlying changes that impact network costs.

To ensure that the hard work put into developing these methodologies is not lost, we believe that Ofgem's decision should include a description of the process that will ensure that they are directly transferred into the RIIO-2 framework. We believe it would be a retrograde step and present an inefficient use of customers' money if the RIIO-ED1 closeout arrangements were reopened and revised as part of writing the RIIO-ED2 licence. We would welcome further discussion on a process to achieve a direct transfer.

Appendix 1 to this letter provides responses to your specific consultation questions.

We welcome any further engagement required following this consultation to support the process of embedding them in the RIIO-ED2 price control.

Yours sincerely

A handwritten signature in black ink, appearing to read 'James Hope', with a stylized flourish extending to the right.

James Hope  
Head of Regulation  
UK Power Networks

Copy Paul Measday, Regulatory Returns & Compliance Manager, UK Power Networks  
Ross Thompson, Regulatory Performance Manager, UK Power Networks

## **Appendix 1 – Answers to specific consultation questions**

### **Question 1: What are your views on our proposed approach to assessing the impact of demand changes, and the cost of reinforcement or alternative solutions?**

The proposed approach recognises and addresses the key drivers for changes in load related expenditure. By outlining a mechanism for identifying and quantifying the impact of these drivers, the proposed approach will achieve its objective of calculating appropriate adjustments to reflect any significant changes.

### **Question 2: Do you agree with our proposal to build on the approach taken at DPCR5 Closeout for load? Do you agree with our proposed approach?**

The approach taken in DPCR5 proved to be successful in making reasonable adjustments that reflected changes in circumstances during the regulatory period that could not be foreseen when setting allowances. Therefore, building on this approach to develop the RIIO-ED1 methodologies is a sensible way to ensure the learning and experience from the DPCR5 closeout is applied to the RIIO-ED1 period. Therefore we agree with this proposal and the resulting approach to closeout for load related expenditure.

### **Question 3: Do you agree with our approach to load indices (LIs)? Is there an alternative you believe we should use?**

As outlined in your consultation document, the load indices are a good indicator of how changes in demand have affected utilisation at primary substations on distribution networks. This makes them a useful tool for assessing the impact of changes in demand, however they do not provide a comprehensive picture of the changes that can impact load related expenditure, such as accommodating distributed generation. Therefore we agree with the proposed approach for integrating an assessment of load indices within the wider assessment of load related expenditure.

### **Question 4: Do you agree with our proposal to build on the approach taken at DPCR5 Closeout for NASD?**

Please see our answer to question 5 below.

### **Question 5: Do you agree with the manner in which we have developed the DPCR5 approach? Is there an alternative approach you believe we should use?**

We agree with the proposal to build on the approach taken for DPCR5 closeout as this ensures the development and learning from that process is captured for RIIO-ED1. We also agree that the proposed approach suitably accounts for the changes that have been made for the RIIO-ED1 NASD process. We do not believe there is an appropriate alternative approach that should be used.

The proposed methodology is an accurate implementation of the reward/penalty mechanism developed in the associated working groups dedicated to this topic. However, paragraph 1.9 of your consultation document states that deficiencies in asset, system or incentive performance data could lead to an adjustment of RIIO-ED1 funding. We understand the importance of data quality in the NASD process but we believe that the significant work in this area has led to a reliable and robust reporting mechanism for risk reduction. Therefore, we do not agree that such a provision is required. In addition to this, there is insufficient information in the consultation document about how this would be assessed and quantified to determine if an adjustment is appropriate.

**Question 6: Do you agree with our proposed approach to HVPs?**

We agree with the proposed approach as it represents an effective way to deal with these large, well defined, projects.

**Question 7: Do you agree with our treatment of the interaction between HVPs and NASD for assessing an outputs gap for non-load related HVPs?**

One of the strengths of the NASD methodology is that it deals effectively with the risk reduction delivered by many types of work relating to a wide range of assets. Including HVPs in this assessment allows the risk reduction associated with HVPs to be assessed on a consistent basis. The proposed treatment for the interaction between this assessment and the assessment of HVP expenditure ensures any resulting adjustments are factored in and ensures there is no “double counting”. Therefore, we agree with the proposed methodology.

**Question 8: Do you agree with our proposal for assessing link box volume delivery?**

The proposed assessment represents a robust way of ensuring that link box replacement volumes have been delivered and a suitable methodology is in place for calculating an appropriate adjustment in the event that these volumes are not delivered. Therefore, we agree with the proposal.

However, the unit cost stated in table X.2 is not reflective of the unit cost used to set the allowances for the SPN licence area. The allowances for SPN were set at the time of Final determination, not the re-opener window in 2017 which used a different unit cost to set allowances for SPMW. Therefore, if an adjustment is required to SPN's allowances, it should be based on the unit cost used to set those allowances which was £4,537 rather than the £5,700 stated in table X.2. We recommend separate values are used in the closeout process for SPN and SPMW to reflect the different unit costs used to set their respective allowances.

**Question 9: Do you agree with our proposal for assessing Shetland costs?**

We agree with the proposed assessment as it deals effectively with the uncertainty relating to these costs at the time of setting the price control.