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Dear David

Independent Distribution Network Operators – Licence applications from affiliates of existing licensees

Thank you for the opportunity to provide a response to the consultation on the licensing of DNO affiliated IDNOs.

It is our view that a DNO affiliated IDNO could be awarded an unmodified distribution licence, and should be allowed to compete with IDNOs and DNOs on an equal basis. We believe there are strong regulatory and legal imperatives in place to ensure DNO affiliates maintain independence, avoid undue preference or discrimination and protect the interests of customers. We believe adequate protection is provided through existing provisions in the electricity distribution licences, the Electricity Act and the Competition Act.

Given the layers of protection currently in place, we are concerned by inferences in the consultation document that the existing framework may not dissuade companies from acting in an inappropriate manner. We note the consultation suggests that one reason a DNO would be interested in setting up an affiliated IDNO company is so the DNO can avoid its obligations to its customers. We are keen to understand more fully the basis of these concerns.

In the absence of further evidence, we feel the additional measures proposed in the consultation document would place an affiliated IDNO at a distinct competitive disadvantage relative to other IDNOs or DNOs and could have a detrimental impact on competition in connections. Where Ofgem has concerns regarding the actions of any licensee we believe there are currently sufficient powers to investigate (under the licence and Competition Act) and take action as appropriate.

There are many legitimate reasons why a company may decide to operate under a separate IDNO licence. When acting out of area, services required may be focused on specific market



segments or developments. As stated in the Ofgem consultation document, IDNO activities tend to focus on smaller networks and mainly serve new housing or commercial developments. This may drive a very different operating model and cost base compared to universal DNO activities, when providing services to all market segments across an entire DSA. We believe it is legitimate that out of area activities may be best serviced through a different and independent structure and management board.

In our opinion the reference to the EDF example is not relevant when considering a DNO affiliated IDNO operating across Great Britain. The competitive connections market has grown significantly since the EDF application was made 10 years ago; there are now 14 IDNO companies and a host of ICPs providing a wide choice for any developer looking for a competitive quote for electricity services. The EDF example was also used as a very specific vehicle designed to service the requirements of the developers of the London Olympic Village and the Ebbsfleet Valley development only, restricting activities to a geographical location and event that is not relevant to a wider context.

In summary, we are concerned some of suggestions raised in the consultation could stifle competition and place an affiliate IDNO at a distinct disadvantage relative to other IDNOs or DNOs. Proposals would create a two-tier system of regulation for distribution network operators. We believe adequate protection is provided under the current legal and regulatory framework to address Ofgem's concerns.

We have provided further detail in response to the specific questions raised in the Ofgem consultation in the Appendix attached. We hope you find this helpful but if you have any further questions please get in touch.

Yours sincerely

Beverley Grubb

Head of Network Regulation

Appendix 1 – Detailed Response to Ofgem Questions

What are your views on the potential impacts on competition in connections and on consumers that we have identified?

We do not believe the entry of an affiliate IDNO would distort competition in the connections market nor should it lead to worse outcomes for consumers. We believe there are legitimate reasons why a company may decide to operate under an IDNO licence out of area, as set out in our covering letter. We believe this could lead to better outcomes for consumers in terms of choice, price, service and speed of delivery of connections.

It is our opinion that the existing licence conditions (combined with wider protection offered under the Electricity Act and Competition Act) offer sufficient protection and ensure no negative outcomes materialise. Competition Law provides for punitive sanctions should it be breached. These obligations and protections apply to both the IDNO and the (affiliated) DNO. We would suggest these sanctions provide a substantial deterrent to any kind of activity that would see the DNO avoiding its existing obligations or try to leverage any advantage for its affiliate.

The consultation also implies that an affiliate IDNO will provide an inferior service for customers relative to the affiliate DNO. We are not clear how Ofgem has come to this conclusion and do not believe there is any evidence to suggest this would be the case.

Are you aware of any other potential impacts on competition?

SSEN is supportive of competition. As set out in Ofgem's previous consultations on competition in connections, competition is generally regarded as leading to better outcomes for consumers in terms of choice, price and services. This aside we are not aware of any other material potential impact.

Do these change whether the IDNO is operating in or outside of the affiliated DNO's DSA(s)? If so, how?

Providing effective controls and balances are in place, we believe the IDNO should be able to operate both inside and outside an affiliated DNO's DSA. Given current obligations under the licence in relation to no abuse of the licensee's special position (SLC4), prohibition of cross subsidy (SLC4) and independence of the Distribution Business and restricted use of Confidential Information (SLC31B), we believe there is currently sufficient protection.

Do you agree with our conclusion that granting a Licence to an affiliate of an existing licensee does not raise any new issues with DUoS charges?

We agree with Ofgem's conclusion. The licensing of a DNO affiliated IDNO will not raise any new issues with DUoS charges. IDNOs generally set charges with reference to the host DNO but are also able to set their own charges. We cannot see how these arrangements would be impacted by the licensing arrangements implemented for affiliate IDNOs.

What other impacts on existing consumers, if any, do you anticipate from granting such a licence?

We believe the main impact of granting such a licence would be on Developers rather than existing consumers. Through increased competition Developers will have increased choice in terms of who provides the electrical network.

Do you think that the current IDNO licence conditions are sufficient to address the concerns raised in this letter?

We believe current IDNO licence conditions are sufficient. As set above, we believe current DNO licence conditions offer substantial protection in terms of the concerns set out in the Ofgem consultation document regarding potential for cross subsidy and lower standards of service. We are concerned by any suggestion that additional restrictions or obligations might be required either on the DNO or IDNO. It is possible this would place the IDNO at a competitive disadvantage relative to other IDNOs and introduce a two-tier approach to regulation.

What additional measures do you think would be required?

We do not believe there is a need for any additional measures to give confidence to the market, customers and Ofgem but if concerns are expressed by others, it may be appropriate to consider arrangements whereby the affiliate IDNO could be required to provide additional information for an initial period or make themselves available for compliance monitoring to give confidence to the market and Ofgem. These powers already exist and so no additional licence obligations are required.

We believe it pertinent to mention proposals linked to previous measures put in place for the EDF IDNO, relating to capturing the 'in area' activity within the DNO price control. We do not believe this approach is appropriate as the DNO's allowed revenue is predicated on existing customer numbers and forecast expenditure for DNO activities only. Any reduction of allowances based on affiliate activity would ultimately disadvantage the existing DNO's customers. It also, perversely, ties the activities of the two companies rather than ensuring independence. We would strongly oppose this approach.

Do you think prohibiting an IDNO from operating within specified areas (for example the affiliated DNO's DSA(s)) would sufficiently address the concerns we have raised?

As set out above, we do not believe these concerns are justified but more importantly, we do not believe it is appropriate to address such concerns by restricting access to markets. We believe all parties should be able to compete on an equal basis, in this case GB wide, and where there are concerns Ofgem should be able to assure itself that the IDNO has demonstrated that they are sufficiently independent and have controls in place to ensure compliance with existing obligations. We are keen to avoid different regulatory arrangements for different classes of network operators.