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Dear Jonathan

Open letter on the RIIO-2 Framework

National Grid has embarked on the task of legally separating the Electricity System Operator (ESO) from the Electricity Transmission Owner (ETO), such that they will be separate legal and licenced entities by the start of RIIO-2. As a consequence, the ESO will respond separately to the open letter and this response is from National Grid Gas and National Grid Electricity Transmission.

Transmission networks have and will continue to provide vitally important energy delivery services which underpin the UK economy and our society. Looking forward networks will also play an important role in facilitating government policy objectives on industrial strategy and clean air through, for example, electrification of UK transport. The exact pathway of future energy evolution is uncertain, but the flexibility that networks offer means that in all credible scenarios they will continue to have a vital role to play long into the future. The scale of change, innovation and investment required to provide safe, resilient, reliable, affordable and sustainable energy delivery to enable a low carbon future will continue to depend on well designed, stable regulation that balances a range of priorities for the long term. The RIIO framework continues to be a good foundation for this and establishing the right overarching objective, regulatory principles and approach for regulating networks into the next decade is of fundamental importance for the RIIO-2 framework review.

In this context, Ofgem's proposed overarching objective for RIIO-2 should be more explicit about the need to balance the competing stakeholder priorities of the energy trilemma and delivery of government's related policy priorities. We suggest the overall aim stated in Ofgem's *Strategy for regulating the future energy system*, represents a more comprehensive statement of the overarching objective for RIIO-2 which is:

"To ensure a regulatory framework that drives innovation, supports the transformation to a low carbon energy system and delivers the sustainable, resilient and affordable services that all consumers need."

We would also highlight that Ofgem's energy system strategy document covers broader issues that closely interact with RIIO-2 price control arrangements and associated obligations (for example gas entry and exit capacity baselines and the broader commercial regime and charging regime) which will inevitably form part of the dialogue with our customers and stakeholders as we work to understand their future needs. Early clarity from Ofgem on what will be in the scope of the RIIO-T2 review versus other work areas in this regard would be welcomed.

The key principles proposed by Ofgem to achieve the overarching RIIO-2 objective would benefit from added consideration and should be further developed as part of this review process. We offer the following suggested builds on the principles outlined in the consultation:

- Giving all stakeholders, including network customers and consumers, a stronger voice in shaping and validating business plans and in defining desired outcomes from networks;
- Aligning the interests of companies and consumers through establishing clear target outcomes, well-designed incentives and the sharing of risks and benefits;
- Clarity on the allocation of risk between companies and consumers which is signed onto ex ante by all parties and ways of managing uncertainty that promotes confidence for companies investors, and consumers;
- Allowing regulated companies to earn returns that are fair and represent good value for current and future consumers, properly reflecting performance delivered and inherent or allocated risks; and
- Providing an ex ante, stable and predictable regulatory regime that attracts efficient financing and investment for the long term.

There are undoubtedly areas of the RIIO-1 framework that can be improved, and it is clear that a central theme for RIIO-2 will be a regulatory regime that can adapt to a rapidly changing market. That said, there are some fundamental cornerstones that we feel strongly should be retained in consumers' interests. These include:

- A totex regime which incentivises companies to reduce total expenditure and which equalises incentives between capex and opex to optimise trade-offs;
- Defining high level outcomes and output goals that all stakeholders are ultimately interested in (as opposed to defining work delivery 'inputs') to stimulate technical and commercial innovation, risk management and efficiency in delivery;
- Setting of allowances, targets, incentives and output goals on an ex ante basis to best simulate the pressures of competition; and
- Mechanisms which flex to encourage responsive delivery of changing customer requirements and minimise potential for windfall gains or losses.

As we look specifically into the RIIO-2 period and based on our initial engagement with customers, consumers and other stakeholders, as well as our own insights, we thought it helpful to highlight our early view of the emerging strategic challenges for our networks and the services they provide to our customers as including:

- The role of transmission networks in facilitating the decarbonisation of transport, particularly through electric vehicles;
- Ensuring the long term health of the existing Gas Transmission network as it approaches the end of its design life whilst fulfilling the short term needs of our customers;
- Ensuring continued resilience of our networks to both physical and cyber threats; and
- Reducing the impact of our networks and our operations on the environment.

Finally, it would be helpful for the RIIO-2 framework review to establish a common language to describe customers, consumers and other stakeholders as there is the potential for these terms to mean different things to different parties.

Specific questions in the open letter have been addressed in our detailed responses below. We hope that these initial comments are helpful and look forward to working with Ofgem and all our stakeholders to shape RIIO-2.

Yours sincerely

[By e-mail]

Chris Bennett

DETAILED RESPONSES TO QUESTIONS

1. Do you agree with our overarching objective for RIIO-2 and how we propose to achieve it?

In our covering letter we set out that the objective would benefit from being more explicit about the need to balance the competing stakeholder priorities of the energy trilemma and delivery of associated policy priorities. We suggest the overall aim set out in Ofgem's *Strategy for regulating the future energy system*, "to ensure a regulatory framework that drives innovation, supports the transformation to a low carbon energy system and delivers the sustainable, resilient and affordable services that all consumers need", represents a more comprehensive overarching objective for RIIO-2. In our covering letter we also set out our proposals for a set of principles for achieving this overarching objective.

2. How can we strengthen the consumer voice (primarily end-consumers), in the development of business plans and price control decisions?

Our networks exist to meet the needs of our customers which ultimately benefit and are paid for by consumers. We support giving all stakeholders a stronger voice in the shaping and validation of business plans to ensure they achieve a balance across a range of competing objectives.

Our current thinking is that we will establish a phased and iterative approach to engaging with our customers, stakeholders and consumer representatives that seeks to (i) establish their priorities and obtain views on how they wish to be engaged, (ii) offer genuine, costed options for material areas of our business plans and (iii) obtain validation and refinement of our holistic business plan proposals that have been built on prior phases.

Our approach will be tailored for different stakeholders and be achieved through the use of, for example, our website, social media, online and telephone surveys, workshops, bilateral discussions, and the establishment of our own expert panels. Drawing on best practice from prior RIIO controls and other sectors, this approach will allow all stakeholders to guide, support and challenge the creation of our business plans and our evidencing of their efficiency and willingness to pay. Ultimately, our aim is to make a submission into the RIIO-T2 price control process that is well supported, reducing the task for Ofgem. There is of course the potential for this approach to be duplicated across all networks which creates a burden on stakeholders and therefore we should look for opportunities to do this efficiently.

Furthermore we think it is important for stakeholders, including end consumer representatives, to have confidence in the way price control parameters are calibrated in order to help deliver our proposed principle of an ex ante, stable and predictable regulatory regime. Ways of achieving this should be explored further in this review.

It would be helpful for the RIIO-2 framework review to establish a common language to describe customers, consumers and other stakeholders as there is the potential for these terms to mean different things to different parties. We define them as follows: customers – those who pay for network services, consumers – the retail energy bill payer and other stakeholders – other parties materially affected by the operations of network companies.

3. How should we support network companies in maintaining engagement with consumers throughout the price control period?

We are proposing to ensure continued dialogue with our customers and stakeholders, including end consumer representatives, through the life of the price control to ensure our ongoing business plans continue to reflect their needs. We will seek views from stakeholders on how to best do this so they can engage on the topics they are interested in and in the manner that suits them best.

Coordinating both the approach taken and, where relevant, engagement activities across network companies should help ensure it is done in a consistent way and would minimise the burden on stakeholders.

4. **Does this structured approach to defining outputs provide the right level of clarity around delivery?**

The structured approach of primary and secondary outputs provides a good basis for delivery clarity. Our recent stakeholder engagement has also reinforced that the current primary output categories remain valid, but we will keep this under review.

5. **How can the outputs framework be improved, including the introduction of additional output categories for example around efficient system operation for distribution network companies?**

The outputs framework can be further enhanced to reflect lessons learned, the needs of a changing energy landscape and to fill any gaps that have come to light in the period. We have identified opportunities for improving elements of the output framework for Gas and Electricity Transmission, both by defining outputs as outcomes rather than specific business plan solutions, and by additional categories to provide more coverage of our business plan looking forwards. There is also an opportunity to reflect on the continuing development of the asset replacement Network Output Measures framework to ensure it strikes a balance of achieving its objectives without becoming overly complex. As interactions between transmission and distribution increase and a whole system view is more important, aligning revenues with achieving outcomes (as per Ofgem's comments in the ET mid period review) becomes even more important.

6. **Did the outputs target the right behaviours?**

Yes, the definition of outputs coupled with efficiency incentives has driven significant benefits for consumers because it has driven behaviours and activities which are in their long term interests. For example - technical and commercial innovation, improvements in asset management capability, risk management capability and work delivery efficiencies by focusing on delivering the overall outcome at lowest possible cost. The benefits resulting from cost reductions in achieving outputs are shared between companies and consumers during the current price control period and following that consumers retain 100% in perpetuity. In the case of load related investment, it has also ensured that planned investments in business plans and associated revenue allowances change in line with the changing outputs required by customers. In some cases, for example in Gas Transmission, we are forecasting the need to deliver more asset interventions and hence spend above our allowances in order to achieve output targets which are necessary to sustain the long term network health. This is an appropriate response created by an outputs regime.

7. **How can we address areas of expenditure for which a clear output is difficult to define?**

It may not be possible to define very specific outputs for all areas of expenditure. In those areas, defining an overall or higher level outcome may be possible to give some linkage between expenditure and consumer benefit. This could be an issue to be tackled in the sector specific reviews as we believe there is scope to further define both specific outputs across a greater proportion of our business plans and for certain categories an overall outcome. For the latter, the example would be consistent with the direction of travel set by Ofgem in its Output Accountability decision for gas compressors where achievement of certain emissions related legislative requirements was the overall outcome that we will be held to account to deliver in the most efficient way we can.

In defining outputs and outcomes we should ensure that the effort and complexity does not drive a level of detail that is disproportionate to the overall value to consumers.

8. **Were the output targets and associated financial incentives set for RIIO-1 appropriate, reflecting what consumers value and are willing to pay for?**

We think the output targets and financial incentives set for RIIO-T1 were appropriate and have acted in the interests of consumers because they have driven continued high levels of network reliability, improved service and cost reductions. We think there is much more that should be done by companies to understand what different stakeholders might value, and testing consumers' willingness to pay in the development of business plans for RIIO-2 and we are committed to an approach for our business plan development that will achieve this.

9. What changes in the RIIO framework would facilitate returns that are demonstrably good value for consumers?

The lesson learned from RIIO-1 is to get much more transparency and clarity up front when setting price controls on outputs, assumptions, expectations and allocation of risks and uncertainties to avoid legitimacy questions later in the control period. Giving a stronger voice to all stakeholders in the price control review process will create a better enduring foundation for trusting that the basis of a price control is appropriate.

A key part of the current framework design that acts to ensure companies are delivering value for consumers is aligning the interests of network companies with those of consumers through sharing of risks and benefits and it is important to retain this alignment.

10. How can we minimise the scope for forecasting errors?

In establishing the ex ante regulatory framework, we should consider the nature of various forecasts included in the price control and determine where the level and nature of uncertainty justifies a more sophisticated approach or whether adding this extra sophistication is counter to the principle of simplification. It would be possible to expand the linkage of certain parts of the price control framework to external indices in an attempt to reduce potential for forecasting error, for example Real Price Effects, although consideration should also be given to the consequences of this for the allocation of risk between consumers and network companies.

11. What constitutes a fair return for a regulated monopoly network company, and how can we ensure that returns remain legitimate in the eyes of stakeholders?

The returns reported by networks are receiving significant scrutiny at present and we think that the legitimacy of how those returns are earned is important for RIIO-2.

What constitutes a fair return should be based upon the risks faced and managed by the networks and the output performance they deliver. It is legitimate for networks to be rewarded for managing both inherent and allocated risks and to earn higher returns as a result of delivering good performance and benefits for their customers and ultimately consumers. To achieve greater levels of legitimacy we think the key issues for the price controls will be the calibration of performance benchmarks, better transparency and understanding of the risks managed by networks to ensure commensurate rewards are given.

An important principle to draw out is that, once risks have been allocated between companies and consumers, the outcome of a risk manifesting as higher or lower than expected is a legitimate outcome and any form of post event adjustment or re-opener undermines the regulatory regime and risks investor confidence which is not in consumers' interests.

12. What factors do you think are relevant for assessing and setting the cost of capital so it properly reflects the risks faced by companies?

Investor confidence in the predictability and stability of the regulatory framework needs to be maintained and this should be a key factor in assessing cost of capital. Changes in policy and long standing regulatory practice would increase regulatory risk and hence the level of required returns, which is not in the interests of investors or consumers. This is captured in our proposed RIIO principle of "providing an ex ante, stable and predictable regime that attracts efficient financing and investment for the long term".

The cost of capital and the broader price control framework need to create the right environment for the investment required to deliver the network consumers want and need into the future. As network investments are long term in nature the allowed return should reflect both the long-term and short-term risks and uncertainties faced by companies. It is therefore imperative that, in setting the allowed cost of capital, regulators do not focus solely on short-term market conditions.

The more exposed networks are to variations in cost, the greater their risk. This risk is not only reflected in how much networks plan to spend in any given price control but also in how much risk they face around that expenditure. Energy networks are facing a broad range of risks, including technological change and changing investment requirements. This manifests itself in both the scale and uncertainty of our investment plans, both of which need to be fully reflected in the assessment of cost of capital. Operational leverage metrics such as the ratio of totex to RAV should continue to be used in assessing the relative scale of investment however they do not adequately reflect the uncertainty and complexity surrounding this investment.

A more detailed example of both the regulatory and investment risk, which is perhaps more pertinent for Transmission than other networks, relates to the multi-year construction period to deliver our investments. Having stable regulation for such investments, both within and between price control periods, ensures that risks can be correctly attributed to those who can best manage them. Any variance in certainty would need to be factored into the allowed return.

13. Can we improve our methods for the indexation of the costs of debt and equity?

We have split our response between debt and equity because we believe that each has its own unique considerations.

Cost of Debt

There are a range of options available in setting parameters around the cost of debt, each having pros and cons. Following extensive consultation RIIO-1 adopted trackers for the cost of debt which has delivered benefits to consumers against a counterfactual of fixed cost of debt. Trackers can be an effective method to ensure that regulatory allowance reflects changes in markets over time. However, we recognise this can lead to outperformance or under performance during an individual price control period. We are therefore open minded about having a discussion with stakeholders and Ofgem about a full range of options, exploring how best to allocate risk. In exploring the options we believe it is important that network companies remain incentivised and able to secure debt which attracts appropriate and efficient interest levels.

Due to the long term nature and scale of the debt carried by the networks it is also important that there is long term stability in Ofgem’s approach to reduce the risks of change which inherently increase the cost. Further to this, alignment across all of the RIIO networks will ensure a level playing field for all networks when they participate in the same debt markets.

Cost of Equity

The overall methodology for allowed cost of equity needs to be considered in the relevant context of the price control for which it is being set and consideration should be given to a full range of options.

In assessing the options consideration will be required on how cost of equity tracking or indexation would work in practice given neither the cost of equity, nor its component parameters, are directly observable or measurable. All parties would therefore need to be confident that any complexity or risk in developing the framework in this area is justified by potential consumer value. Nevertheless, we are open minded to exploring the options with Ofgem and stakeholders.

The key consideration for both the cost of debt and cost of equity methodologies is that there is a clear understanding of the implications for network risk and the allocation of risk between shareholders and consumers.

14. Are there specific amendments to any core aspects of financeability that we should be considering in light of performance during RIIO-1 and the change in the financial environment?

Company financeability is a critical consideration for any price control since it impacts not just the companies but the costs borne by the consumers who will pay for the long term financing costs of the networks. The revenue profile and consumer bill volatilities across the price control should also be considered in conjunction with financeability.

We agree with Ofgem that the level of WACC is key to financeability given inevitable uncertainty and welcome the proposed review of tax, capitalisation and depreciation approaches because they all have an important bearing on financeability.

During this review it is important that Ofgem's approach does not focus solely on the notional company structures and reviews actual company structures to ensure there are no unintended consequences of the proposed approach. There needs to be an equitable balance between theoretical and practical with, for example, the realities of the processes and metrics adopted by the major ratings agencies factored into the approach.

15. Should we consider moving to CPIH (or another inflation index) and how should we put into effect any change to ensure it is present value neutral for investors?

As Ofgem has rightly identified, the potential adoption of CPIH needs to be managed carefully because it can have significant ramifications for consumers (intergenerational cost impacts) and investors (through the introduction of regulatory risk). We consider that there needs to be a full assessment of the need to move away from the well-understood RPI and a detailed review of the potential impact of introducing CPIH before a final decision is made to ensure that the implementation is value neutral for investors and that the consequences for consumers are desirable.

We recognise that other industries may have adopted CPIH prior to Ofgem, and we will be able to draw much from their implementation. However there are likely to be important differences in the RIIO framework that will need to be considered.

16. Do you think there are sufficient benefits in aligning the electricity price controls to off-set the disadvantages we have outlined?
17. Are there any other realignment options we should consider?

The RIIO framework review should consider more fully the pros and cons of aligning price controls both within and across sectors, either for the start of RIIO-2 or potentially RIIO-3. Further work is required to set out and attempt to quantify the advantages and disadvantages. We note that alignment of price controls is not the only way of achieving whole system optimisation benefits. Significant progress has been made through a number of ongoing initiatives, such as the Energy Networks Association's Open Networks Project.

18. What amendments to the RIIO framework, if any, should we consider in supporting companies to make full use of smart alternatives to traditional network investment?

The current framework for transmission goes a long way to delivering smart alternatives, with evidence already available in RIIO-T1 to support this. We encourage the exploration of further incentives to support this area, possibly in charging, storage licensing and balancing service markets as well as an evolution in approach that seeks to define and value outcomes, as opposed to outputs, as set out above. We should also explore an explicit incentive to encourage whole system thinking and smart alternatives across the transmission and distribution network boundary, which would encourage more innovation in this area.

Greater transparency in the electricity transmission Network Options Assessment process would help stakeholders to see where smart solutions and associated benefits are being delivered. The potential for expanding the remit of such a process from transmission into distribution should also be considered.

19. Given the uncertainty around demand for network services, how much of an issue might asset stranding be and how should this risk be dealt with?

Despite radical changes in the energy market, the electricity and gas transmission networks will continue to play an important role in facilitating secure energy delivery and supporting the transition to a low carbon economy through the RIIO-2 period and beyond. The uncertainty therefore may not be so much about demand for network services, as to what the capabilities of networks need to be in the future.

We think the magnitude of the potential for asset stranding should be assessed as part of the RIIO framework review and careful consideration given to the treatment of that risk, whether it is borne by companies, consumers or a combination of the two and the corresponding implications for allowed WACC. Assumed regulatory asset lives are a key consideration in this topic area.

There is also an interaction of risks that sit with network customers through the levels of user commitment that prevail across the gas and electricity market regimes. This links to our earlier point about being clear on the scope of the RIIO framework review in relation to interactions with gas and electricity market frameworks (e.g. gas entry and exit capacity baselines and the broader commercial and charging regime).

20. How do we need to adapt the RIIO framework, and the uncertainty mechanisms in particular, to deal with this uncertainty?

The RIIO framework review should consider which elements of networks' responsibilities are the subject of major uncertainty, what the likely triggers of change are, and whether these areas could be treated differently from areas where greater certainty exists. Any uncertainty mechanism is inevitably optimised to work within an envelope and so reviewing how well existing mechanisms have operated against the shifts that have occurred since RIIO-1 would also be useful input to this assessment.

21. Is an eight-year price control period with built-in uncertainty mechanisms still appropriate given the greater range of plausible future scenarios? What has an eight-year price control period allowed network companies to accomplish or plan for that would not have occurred under a shorter price control period?

A longer price control period gives more scope for companies to innovate and drive efficiencies as the pay-back period is greater and therefore more ambitious options, perhaps with longer implementation lead times, are taken forward. Examples include both technical and commercial innovation, one of which includes our complete overhaul in approach to circuit breaker replacement.

The downside of a longer control period is that deviations can occur from original assumptions for those elements of the control that are subject to more uncertainty and these deviations can lead to the potential for windfall gains or losses. The critical factor for the RIIO framework review is therefore whether uncertainty mechanisms can be designed to deal appropriately with these uncertainties rather than focusing on the length of the control period itself.

22. What improvements should be made to the assessment of business plans?

Ofgem currently use a comprehensive approach for assessing business plans but there can always be improvements made to the processes to better reflect the characteristics of networks overall and the individual differentiators across sectors. A stronger consumer and broader stakeholder voice in the assessment of business plans will be beneficial, alongside transparency from Ofgem on the decisions made throughout the assessment.

23. Should we give further consideration to companies' historic performance against their business plans?

Analysing historical performance against the RIIO-1 control is one element to consider. It should be recognised that our business plans have changed very significantly, driven by huge changes in the external environment and the needs of our customers since the original RIIO-T1 business plan was submitted so a comparison back to the original business plan itself may not prove that useful. We are also conscious that the challenges ahead may be different in nature to those that companies have responded to over the RIIO-1 period and therefore caution placing too much weight on backward looking analysis.

24. Should we determine the revenues an "efficient" network company requires before seeking information from the companies themselves?

There is likely to be limited scope for improvement derived from Ofgem undertaking an assessment prior to network submissions. Our plans for building a stakeholder led submission are fundamental to building our well justified business plan. It is unclear how this could work with an approach where Ofgem determines the revenues of an efficient network company before seeking information from the companies and therefore the views of their stakeholders. All available data should be used by Ofgem to inform their assessments including the network's stakeholder led submissions.

25. How well has the IQI and efficiency incentive worked in revealing efficient costs through the business plan process and encouraging efficiency throughout the price control period?

IQI seeks to incentivise ambitious business plan submissions, and the strong totex efficiency incentive (derived from IQI) with an outputs based regime through the control period is proving very effective in driving National Grid to improve efficiency and deliver benefits which are shared with consumers both within the period and into perpetuity.

26. What alternative approaches could we consider to encourage companies to give us high quality information which minimises the damage from their information advantage?

We take our responsibilities to provide Ofgem and the industry with the best information we can seriously and we endeavour to be as accurate as possible regardless of the incentives and we will continue to do this.

Annual regulatory reporting packs and performance reporting over the RIIO-1 period have built up a considerable historic data set and our open approach to stakeholder engagement gives all parties the opportunity to test our forward looking assumptions and improve them. We will work with Ofgem and the industry to develop any suggestions for how we might provide additional confidence.

27. What impact has the innovation stimulus had on driving innovation and changing the innovation culture?

The pace of industry change is unprecedented and 'whole system' development, in particular, is of critical importance. RIIO does incentivise networks well over the control period, but innovation stimulus provides an important incentive for projects which deliver over a longer period and where outcomes are much less certain. These incentives have allowed networks to undertake more ambitious work and focus on big scale innovation and associated culture change derived from undertaking this work by addressing the risk/reward imbalance of innovation in a price control environment.

A lack of innovation stimulus would make the business cases for innovation more difficult, which seems at odds with the challenges currently facing the industry. For example, our Offgrid Substation Environment for the Acceleration of Innovation Technologies project at Deeside would not have been possible without innovation stimulus and in a shorter price control period.

28. Have the incentives inherent in the RIIO model encouraged network companies to be more innovative and what should we consider further?

The RIIO framework includes strong incentives for network companies to innovate for greater efficiency through:

(i) the focus on outputs – giving companies freedom to innovate in delivering the outcomes customers and consumers want

(ii) sharing factors – where consumers and network companies share the benefits of innovation

(iii) the totex mechanism – allowing for unbiased trade-offs between capital and operational expenditure

(iv) an 8 year duration – providing a sufficient period for the company to retain a proportion of the benefits of innovation before they are reset at the next price control review (benefits which consumers retain in perpetuity)

Innovation for greater efficiency has delivered value to consumers, both in the short term through immediate savings and in the longer term through revealing a new level of efficiency for all future work. Nevertheless, we think an innovation stimulus mechanism still has an important role to play going forward, especially given the challenges faced into the RIIO-2 period, as the aforementioned incentives inherent in the RIIO model alone are unlikely to deliver the big scale innovation required.

29. Do you agree that the scope of competition should be expanded in RIIO-2?
30. What further role can competition play?

National Grid is committed to delivering best value for consumers and utilises competitive tenders to secure best value. Price controls with the right mechanisms such as RIIO, which provides a proxy for competition, has incentivised companies to act competitively and ensured value is delivered for consumers. RIIO-2 is the opportunity to build on the success of RIIO-T1 in this respect and will offer the opportunity to reset the key (risk/return) price control parameters.

We continue to believe that the use of competition, where demonstrably beneficial for consumers, has a role to play in the provision of energy networks. We agree with Ofgem that the application of competition to new, high value and separable projects is where it is likely to be most beneficial to consumers. To maximise its effectiveness suitable projects for competition should be identified on a case by case basis, backed by a risk assessment and clear cost-benefit analysis.

31. Which elements add the most complexity and how do you think that these and the broader RIIO framework could be simplified?

The industry is inherently complex and the onus is on all parties involved in the process to translate and simplify that complexity for stakeholders. The challenge lies in balancing the need for new ways of managing uncertainty and other elements of the framework that deliver positive outcomes for consumers, but naturally introduce additional complexity, with the benefits that simplicity brings. Greater transparency in all aspects of the ongoing process should sit alongside and may sometimes be a substitute for simplicity.

Much of the current complexity has arisen from load related aspects of the framework, where the generation background has changed considerably since the start of RIIO-1 and this should be a focus area for how we set uncertainty mechanisms in RIIO-2. Going forward, as new elements of the RIIO framework are developed, each aspect should be carefully considered as to whether any added complexity is justified. Asset health expenditure is an example of an area that should be capable of more clarity without additional complexity. We also think the financial timing lags and iteration process within the financial model should be reviewed as this is another area of significant complexity.

32. What improvements could be made to the format and presentation of the business plans?

Greater consistency in company business plans, especially in terminology, would be beneficial and common presentation for elements will make them more accessible and comparable. The possibility of tailoring business plans for use by specific stakeholder segments should be considered as an additional measure to enhance their accessibility. A pre-defined template would enable easier comparison of business plans across companies. The extent of standardisation should be balanced against ensuring network companies have the freedom to structure and express their overall submissions in a way that represents and will resonate with the stakeholders with whom they have co-created it.

33. Should the plans be revised at any stage during the price control, for example annually?

In common with other companies we update our business plans on an annual basis and are exploring how we can do this with even stronger stakeholder input and transparency in future. However, the purpose of more frequent, formal revisions is unclear and it is important that any revisions of plans should not undermine the effective incentivisation of ex ante allowances over the price control period and the savings these allow network companies to deliver for consumers.

34. Should we retain fast tracking and if so, for which sectors?

Ofgem should undertake a review of the benefits of fast tracking in RIIO-1 to help answer this question as it is not transparent to us whether the rewards allocated to fast tracked companies are commensurate with the overall consumer benefits derived. In the meantime we intend to develop our business plans and prepare our RIIO-2 submissions in a manner consistent with that which fast tracking seeks to encourage.

35. Do we collect the right information in the right format and are there better ways to monitor the performance of companies?

We recognise the need for Ofgem to collect network company performance data but welcome Ofgem's signalled intent, through the trial of a Strategic Performance Overview report to supplement RRP this year, to seek to more high level management information about company performance as opposed to increasing quantities of data which may be more difficult to interpret.

36. What are your views on how the changing role of the electricity SO should be factored into the RIIO framework, including whether or not the electricity SO should have a separate price control?

Following legal separation the National Grid Electricity Transmission Owner (TO) and System Operator (SO) will be separate legal entities and will need to have separate licences. Whilst the SO shares many common objectives with TOs and DNOs the role that it plays and the way in which it carries out this role is significantly different.

In addition to these differences, the SO will also need to be appropriately funded for the role it carries out. For these reasons a separate price control is appropriate. The principles of RIIO are a strong basis upon which to develop this price control.

37. Do you agree with our broad stakeholder engagement approach set out above?

We agree with the proposed approach and look forward to contributing.