

EUA UN Response to the RIIO-2 Draft Determinations for Transmission, Gas Distribution and Electricity System Operator

About us

The Energy and Utilities Alliance (EUA) provides a leading industry voice helping shape the future policy direction within the sector. Using its wealth of expertise and over 100 years of experience, it acts to further the best interests of its members and the wider community in working towards a sustainable, energy secure and efficient future. EUA has seven organisational divisions - Utility Networks (UN), the Heating and Hotwater Industry Council (HHIC), the Industrial & Commercial Energy Association (ICOM), the Hot Water Association (HWA), the Manufacturers' Association of Radiators and Convectors (MARC), the Gas Vehicle Network (GV Network) and the Manufacturers of Equipment for Heat Networks Association (MEHNA)

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Response

Summary

EUA understands that Ofgem need to balance a wide variety of factors in determining the Price Control Determinations. Balancing the needs of consumers to keep energy bills affordable, safety, reducing carbon in line with our net zero commitments and providing space for innovation and service improvements.

However, in conversations with our members, who range from the gas distribution and transmission networks, to multi-tier supply chain companies, we do not believe that the proposed price control draft determinations (PCDD) are fit for purpose.

Our concern is that in setting an extremely limiting PCDD Ofgem will prevent the networks from delivering what is expected of them, it will prevent them from innovating, bringing new solutions to meeting net zero and it will harm the very consumers Ofgem is saying it is acting in the best interests of.

We urge Ofgem to listen to the responses to this consultation and make changes to the PCDD to ensure the networks can operate to the best of their abilities.

Net Zero Target

Rapid progress is needed towards Net Zero and the networks will play a leading and central role in meeting these targets, through developments in Hydrogen, Green Gas and Whole Systems Solutions. The Networks are ideally placed to help solve some of the biggest problems we face in trying to decarbonise heat and transport. Over the last eight years the networks have pioneered work on green gas, hydrogen and hybrids. It is very likely that without this work we would be even further behind our targets to reduce emissions. Ofgem's proposals fall far short of providing the framework and tools that the networks need in order to take this from concepts and trials to working realities.

Ofgem could have provided an opportunity for the energy networks to lead a green economic recovery. But the route Ofgem has set out in the draft determinations will delay much-needed investment and miss the chance to create jobs and sustainably develop much needed skills right across the country.

Rather than accelerating the UK's transition to net zero, the delays to new projects caused by the draft determinations will slow our progress in a period where every year counts, and we will be spending less on developing new low-carbon technologies.

For gas, the draft determinations derail our progress in trying to ensure the UK is hydrogen ready. As a new technology, hydrogen requires the networks to take on more risk and invest more in building up the UK's supply chain capability. Ofgem has failed to recognise that developing new markets and our network to transport hydrogen is not business as usual innovation and have cut the innovation allowance proposed for investing in technologies by 20% compared to RII0-1. This will lead to delays of as much as £150m of investment in preparing the country for a hydrogen transition, delaying the point at which major decisions on the future of the energy system can be made.

Furthermore, the mechanism for access and the funding threshold is not conducive to agile and flexible R&D needed to reach Net Zero. The high funding threshold means the projects to decarbonise heat, power and transport will not qualify for funding.

Although we support the principle of a Net Zero reopener, several changes are needed to make it more able to support the sort of projects required to help decarbonise heat. This includes a lower threshold for the reopener, the ability to aggregate projects together and a trigger mechanism that network companies can use.

Ofgem's exclusive right to trigger the Net Zero re-opener could unnecessarily delay investment. Network companies will have to make representations to Ofgem about a relevant change in circumstances in order to prompt Ofgem to undertake a series of consultations before amending the network companies' licences to implement any adjustments deemed appropriate. Networks should be allowed to trigger the Net Zero re-opener.

Heat decarbonisation projects start small and are then scaled up. It's important the mechanism reflects this, with a lower re-opener threshold for qualifying projects that also applies to aggregated projects.

Networks hold the data and insight into energy systems, and we require networks (not just Ofgem) to be able to trigger a reopener mechanism to give more certainty around network investment decisions.

EUA is also concerned around the potential funding for the Iron Mains Replacement Programme, which is a key part of 'no regrets' future energy planning investment. Ofgem need to ensure appropriate funding; reinstating the expenditure which has been disallowed in the draft determinations. In the draft determinations GDNs have been allowed no investment to replace any of these assets before 2026. The implications of this decision have not been reflected in maintenance and repair costs, nor has the impact on customers from increased interruptions and costs been assessed, and neither has the environmental damage from this decision been considered. In some instances, GDNs would be unable to meet statutory requirements if this was not resolved and would have little choice but to pursue the appeal option. More complex (and more costly) work remains for GD-2. If price controls don't reflect this there will be significant challenges to future network investment and programmes. Coupled with these challenges are the potential impacts of Covid-19 and Brexit taking place at the same time.

The Iron Mains Replacement Programme keeps the gas flowing safely today and prepares the gas network for a decarbonised future – making sure it's ready for green gases like biomethane and hydrogen. This equally applies to allowing the gas networks to use work done in industrial clusters to be passed onto consumers through reduced emissions. We are concerned that Ofgem may not allow the networks to use hydrogen for example generated in the clusters to be fed into local grids.

Innovation

We understand the rationale behind trying to make innovation more of a Business As Usual (BAU) process. There have been occasions where innovations have not been used or taken up by network companies. However, these are the exceptions. The innovation process in RIIO-1, whilst not perfect, did stimulate billions of pounds of investment into innovation in both large and small projects. All which have helped transform the UK networks into the most forward thinking and effective networks in the world. This process also supports thousands of UK jobs which will be vital in rebuilding the economy post Covid.

We had always argued that the innovation process needed tweaking not dismantling. However, it appears that Ofgem have ignored those comments and instead decided to seriously curtail the amount of jobs and investment that will be allowed for innovation.

This will lead to job cuts and possibly companies going out of business, at a time when innovative energy supply chain companies are most needed. Instead of becoming a world leader in energy innovation capable of exporting our expertise around the world, we will no longer be in this position.

We consider that the £5m minimum spend is very restrictive and may result in projects not being taken forward via NIA. We suggest that the threshold is removed and set on a case by case basis as each Innovation challenge is released.

Applying a blanket requirement for peer review or an independent audit of every project may not provide the best use of resources and may create cumbersome processes that do not lead to desired improvements.

The PCDD is not clear on how the innovation process will work within RIIO2. We need clarity in order to educate the supply chain and to determine what issues may arise. It is important to note that a large number of suppliers that work with the Networks do not understand all the minutiae of RIIO and how the process works. Often, we only discover problems with the

process once work starts. This will be even more complicated if the PCDD is not clear from the outset.

One of our principal concerns is that the process now could become too top down. If Ofgem are planning to control the process and have a greater say on what innovation is valid and what is not, this could lead to inertia and a curtailment of more specialist innovation that Ofgem may not have the inhouse expertise to evaluate correctly.

This coupled with additional quality assurance requirements will almost certainly mean SME's are excluded from the process which will again reduce innovation but also cut jobs and specialists from the sector, just at this critical stage for net zero.

It is not clear from the PCDD if there will be a right to appeal for unsuccessful innovation bids, this could reduce accountability and a willingness to engage in the process. It will also remove a potential learning opportunity for unsuccessful bids.

We are pleased that funding from RIIO1 can be rolled into RIIO2, this removes a potential cliff edge scenario. However, we will also now need assurance over the process for RIIO3 given the shorter obligation period of 5 years.

There are a lot of experts currently working on supporting innovation for the energy networks, they have spent the last few years engaging with Ofgem on stakeholder panels and working groups. They had hoped this work would have been reflected in the PCDD and that learning used to improve the innovation process within RIIO. The frustration is that this is not the case and that advice has not been taken. EUA are concerned that this may force these people and organisations out of sector which would severely reduce our capacity to support innovation and also bring forward the necessary changes that will be needed to meet net zero. We urge Ofgem to look again at the PCDD for innovation.

Fuel Poverty

Ofgem, in total, has proposed a curtailment of projects worth almost £164m in benefit to vulnerable customers, which would have had a total cost of approximately 30p on each annual gas bill, according to work done by the NEA. Each rejection is based solely on the basis that they could be done through the UiLiA. However, this will not be possible.

Ofgem have not previously stated that it this would be the only funding mechanism available for projects focussed on vulnerability. Ofgem have moved in this direction without any engagement of its stakeholders.

Fewer projects helping vulnerable customers will happen during the price control, and therefore households that are struggling the most will receive less value than proposed.

We don't understand how Ofgem could have come to this decision. Having committed to giving consumers a stronger voice in business plans, Ofgem has not demonstrated this in the draft determinations. The wealth of stakeholder input used to build the plans appears to be almost entirely disregarded, and Ofgem has provided no detail of consumer or broader stakeholder consequences of the draft decisions they have made.

Overall the package of the draft determinations delivers an extremely worrying lack of incentivisation or ability to deliver for consumers.

Again, we call on Ofgem to review their decision-making process on this. If the very groups set up by Ofgem in order to bring consumer voices into the planning process called for more support for vulnerable and fuel poor households, how can Ofgem then reject these voices? It, perhaps unfairly, will lead many to assume that the decisions on the PCDD were made ahead of the whole consultation process and will definitely lead to less engagement in the future given the lack of adoption of recommendations made through it.