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Sent by email to: FutureNetworkRegulation@ofgem.gov.uk

Dear Akshay

Open Letter: Future Systems and Network Regulation

Electricity North West Limited (ENWL) is one of six electricity distribution network operators (DNOs) in Great Britain. We are responsible for maintaining and upgrading £12bn of electricity infrastructure across the North West - 13,000 km of overhead power lines and more than 44,000 km of underground electricity cables and much more. We deliver over 25 terawatt hours of electricity through our network relied on by over 5 million people across an area of 12,500 square kilometres and invest £1m per day to provide a reliable, affordable and sustainable network. This covers the diverse communities between the Lake District to the city of Manchester and all the cities, towns and villages in-between.

The approach of ex-ante, incentive-based regulation has and is serving customers well and is enabling investment as well as significant improvements in the levels of service and is achieving these at low cost. Indeed, internationally, the GB regulatory approach is extremely well regarded.

Ofgem's Open Letter raises fundamental questions as to how regulation is taken forward. There are several reasons why it is important that Ofgem continue to ask questions, primarily these reasons are the changes in the level of investment and innovation required to deliver efficient networks that can meet the significant challenges of the transition to net zero and the long-term risk of stranded assets as markets for consuming and, therefore, delivering energy change. Any considerations of change should be tested against these key new challenges and Ofgem's ongoing primary duties.

Net zero is bringing many changes to energy markets and the way in which energy will be consumed. Therefore, the networks tasked with delivering this energy must be able to meet new needs and adapt to these changes. Supporting the transition to net zero requires significant levels of investment in an environment of innovation and adaptability.

So, whilst we support this open letter and Ofgem seeking views, evidence of key problems that Ofgem is seeking to address is not presented clearly. The open letter introduces a potential scale of change to the successful fundamental principles of the regulatory regime, but does not make a clear case for why such change might be needed. The case for change would provide the vital evidence



that would enable all stakeholders to test whether a new proposition will be an improvement compared to the status quo, by showing the weaknesses of the status quo and where improvement is required. Such analysis is missing from the open letter.

Absent evidence of the need for a change in fundamental principles, focus should be on whether the current ex-ante incentive based regulatory approach can be evolved and developed to meet new challenges. Since privatisation and particularly during the transition from RPI-X to the RIIO framework, the current regulatory regime has demonstrated an ability to evolve and improve while ensuring the continuity of a series of essential fundamental principles. This approach of combining evolution with consistency is strongly in consumers interests.

Focus therefore turns to continuing to evolve Great Britain's world leading ex-ante incentive focused regime. There may be a number of insights that can be gained from observing how RIIO is operating and expected to work in RIIO-2, including some of the features of other approaches Ofgem highlights for consideration in the Open Letter.

Reflecting on our experience through developments for RIIO-ED2, Ofgem is identifying how it considers the regulatory regime should evolve and on the back of this, Ofgem is implementing material changes. This includes developments such as a Returns Adjustment Mechanism. Ofgem has also recently talked about reviewing how inflation is treated and indicated it could propose changes, demonstrating the potential for adapting the current regime. Ofgem has also brought in Price Control Deliverables and bespoke mechanisms to RIIO-2 controls. Furthermore, the new LOTI and MSIP processes for particularly material transmission investment decisions are effectively mini price control evaluation and allowance setting processes. Ofgem clearly does engage in the active consideration of potential developments, including for a bespoke incentive¹ being in place to benefit our customers, which we consider could be rolled out to other energy price controls and also to other sectors in due course. It's strongly evidenced therefore that the current framework can and does evolve, and is developing.

Other regimes do have facets that should be more deeply evaluated by Ofgem. For example, the American approach to regulation (Rate filling) involves regulatory scrutiny of companies financing arrangements, particularly debt raising, where the regulator has to give some degree of pre-approval. In our discussions with Ofgem on financing matters, particularly on debt, a view advanced by Ofgem has been that regulators cannot evaluate company financing decisions, but clearly this does occur in other jurisdictions. The benefits and costs of adopting a different approach to financing choices should therefore be explored more fully. Indeed, with the fracture between a period of low interest rates and the current rate reversion that has taken place, now is the time for Ofgem to review its approach to financing aspects of price controls because there is a such paradigm shift in the circumstances.

We participated in a Citizens Advice project that has considered how to evolve regulation going forward. The recommendations can be found here², several of which resonate with us and could improve outcomes for consumers. Importantly Citizens Advice finds, **"While the current price control framework, known as 'RIIO', is largely viewed as positive, there are changes needed to make it fit for the future."** We agree with an evolutionary approach.

¹ ENWL uniquely proposed Dig, Fix and Go, an innovative stakeholder led approach to reduce emergency roadworks disruptions for customers that Ofgem proposed accepting at Draft Determination stage.

² [Future Network Regulation: Delivering a regulatory framework fit for the future - Citizens Advice](#)

Finally, should Ofgem conclude reform on the scale potentially contemplated is after all required, it is important to plan this carefully as it could take multiple years and might even need legislative change. This would need to be combined with complex and careful change management involving all stakeholders, be they investors, consumers and other stakeholders so the effective delivery of essential utility services continues and any targeted outcomes from reform can be achieved in parallel.

More detail is provided in the appendix that follows. We are happy to discuss our response in more detail if you have any questions.

Yours sincerely

A handwritten signature in grey ink, appearing to read 'PB', is positioned above the printed name.

Paul Bircham

Engagement and Strategy Director

Appendix 1

- Should a standard approach to regulating networks through a common framework (RIIO-3) or more sector specific?
 - Because the sectors are now increasingly different with gas networks needing to make a transition to hydrogen, or face the potential for asset stranding, now is the time to evaluate the potential need to take regulation in different directions for gas networks. This might potentially apply from RIIO-3, but this will be challenging to do in the time available, unless Ofgem heavily prioritises this. The high levels of investment and strong performance improvements from electricity networks show that the RIIO framework continues to be appropriate for electricity distribution which is essentially accelerating and growing.
- Periodic reviews or more regulate as you go?
 - Periodic reviews have significant advantages and underpin ex-ante, incentive based comparative regulation. In transmission Ofgem already does use a more, “regulate as you go” approach for major projects. These large transmission projects, some of which might be as material as a whole DNO price control period funding, definitely merit specific regulatory processes as and when they are timely. This is for us an example of how the current approach to regulation is adapting to a need for a number of large transmission investments coming forward.
- Are steps needed to speed up decision making in a period of greater change?
 - Yes, but the steps needed require Ofgem to be more comfortable with uncertainty and risk in its decision making. Ofgem must not be tempted to apply hindsight and should not penalise companies making decisions in a timely way, but with imperfect information about the future. Certainty of picking the right choices has challenges if decisions still need to be speedy. We therefore believe Ofgem’s choice to be involved in making the major decisions on transmission projects before they are built is appropriate. We believe Ofgem should consider being involved in other elements of decision making that are material for consumers including some financing aspects (e.g. debt raising).
- Are process changes required?
 - Yes, more notice of customer and stakeholder engagement should be taken by Ofgem and greater clarity be provided on how these are insights are used by Ofgem is essential. We suggest more work by Ofgem on the detail of engagement takes place sooner, preferably between the intensive price control setting processes, so Ofgem can be confident in the insights achieved. Ofgem may even determine that it needs to take the lead itself in more customer and stakeholder engagement, so that it can then be able to rely upon it.
 - Between sector price controls we suggest the price control teams are retained focussed on that sector and work on the developments to the regulatory framework that are required for the next price control, so the price control setting itself becomes more focussed on policy and mechanism implementation and to recognise that there are increasing differences between the sectors. RIIO-ED2 is proving a challenging and substantial task as both setting a new price control and developing a range of complex and interlinked new regulatory mechanisms is all happening at the same time. A practical example is on load related expenditure where looking ahead to any future foreseeable changes could be pre-developed.

- Is something broken that means integrated energy system decisions are not being made at a time these are becoming more important?
 - No, existing mechanisms can be adapted and there are wider issues such as the resourcing available in local authorities. We request Ofgem's concerns be more clearly evidenced and greater transparency be shared on potential issues before remedies can be identified. Our experience to date is that this opportunity of greater integration of decision making should be explored, though we get mixed messages on how far and fast Ofgem wants us to go on this, even where the stakeholders have told us what assistance they need. We put forward as ENWL a specific ED2 UIOLI approach to net zero advice and co-ordination with businesses and enhanced support to local authorities. At the Draft Determination stage Ofgem has rejected this. This measure we put forward, strongly supported by our stakeholders, should, we contend, be accepted at final determination stage.