



Independent Networks
Association

Jane Dennett-Thorpe

Ofgem (emailed to FutureNetworkRegulation@ofgem.gov.uk)

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Dear Jane

Consultation on frameworks for future systems and network regulation: enabling an energy system for the future

I am writing on behalf of the Independent Networks Association (INA). The INA represents and consists of Britain's leading independent utility network owners and operators who serve the domestic, commercial, and industrial sectors across GB.

We welcome the opportunity to input on the topic of future systems and network regulation. Any changes to the regulation of networks will impact the relative price controls of the Independent Network Operators (IDNOs) and Independent Gas Transporters (IGTs), which could affect the stability and predictability of charges for IDNO and IGT customers. The development of competition from the independent sector has brought benefits to customers through challenging incumbent operator's performance and delivering new and innovative solutions to meet industry challenges. Because of this our members have a strong interest in ensuring that a wider range of stakeholders and customers can continue to enjoy these benefits through any regulatory changes to the planning and delivery of networks. Our members also recognise the need for transformation and agree with the strategic need for changes to network regulation to place the sector on the right path to meet the country's net zero targets.

While we broadly agree with the proposed analytical framework intended to assess the options and their application to the various archetypes and building blocks, we believe there should be principles that underpin the chosen options, not as a blocker or criteria for selection but as a function of the end-design of the framework.

Principle 1: Retaining and fostering effective competition

We note that competition is outlined as a potential mechanism for delivery of certain outputs/needs. This can, and has been shown to, reduce costs, lead to agile delivery and improved service levels and customer satisfaction, and deliver more rapid growth. Our members have delivered these benefits through a genuinely competitive market where outcomes are driven by customer choice, and it is important that any new frameworks do not inhibit this competition. Where there is existing customer choice, we believe that it is preferable to allow the market to determine the most efficient outcome. Though the independents primarily operate at the lower voltage tiers, we note the risk of a central agent or plan focusing on incumbents and the higher voltage tiers, potentially to the



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detriment of the lower tiers. We believe it is important that the competitive process for independents to bid and operate networks should continue to be supported with independents retaining the ability to innovate in designing local energy network solutions.

Principle 2: Minimising information asymmetry

We believe that any framework should incentivise the reduction of information asymmetry. This would have the dual effect of reducing friction and enabling smoother and well-rounded analysis and forecasting of strategic needs but also reduce the costs associated with a monitoring framework. Improved data transparency would allow more parties to compete in segments where competition is allowed. Customers would ultimately benefit from these improvements, particularly where a post-monitoring regime has less stringent needs and has less resource requirements than the status quo.

Principle 3: Ensuring continued stability

The current ex-ante regulation price control has the benefit of allowing investors to understand the returns available on their committed capital. The new framework should seek to maintain that ability or risk an increase to network operators cost of capital at a time where there is likely to be a significant requirement for capital to deliver the transition to net zero. Any increased costs will ultimately be borne by energy consumers. For the independent sector, the current relative price control secures customer benefits but also provides stability and transparency for financing, leading to improved competition within the sector.

Considering Ofgem's analytical framework and complementing these with the principles noted above, we would support a framework akin to that of Electricity Transmission. Utilising archetype 2 as the primary building block for regulating electricity distribution while ensuring the strategic outputs are determined by the Future System Operator (FSO) as in archetype 1. This would result in a framework of reduced complexity due to the nature of archetype 2 compared to the RIIO price control and would ensure that strategic investment is considered and mandated with a holistic perspective.

There are some risks inherent with the structure of archetype 3 which we think should be considered prior to inclusion as a building block for any part of the framework. A key risk is the terms on which the ex-post monitoring regime would be set up. Though a benefit may be realised in terms of the resource required from price control participants and the regulator at the outset, this is only possible if a lighter appraisal post-project completion is used compared to the current up front in-depth assessments. However, ex-post regulatory intervention will require a high threshold for burden of proof. Combined with lower investor certainty due to potential intervention, we think the costs may outweigh the benefits in the short and medium term.



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Lastly, we are conscious that there are a range of areas currently being reviewed with a view to reform these in the medium term such as Local Energy Institutions, Distributed Flexibility and the Distribution Use of System Significant Code Review. There is an interplay between these areas which may bring to light additional benefits or costs not already considered. We would welcome further detail on Ofgem's thinking on the planning, timescales, and milestones for the interlinked areas which would allow for any associated risks to be understood. Additional benefits are likely to be materialised where these reviews are aligned and unified outputs are sought.

We have detailed our responses to specific consultation questions in the appendix to this letter. Please let me know if there are any questions on any area of our submission.

Yours sincerely,

Nicola Pitts
Executive Director

Appendix 1: Consultation Questions

Q.1. What should the role of the ‘consumer voice’ be and through what institutions and processes should it be channelled?

Q.2. How detailed could an independent, cross vector view become to determine future plans for periods beyond RIIO-2 and support effective use of the ‘Plan and Deliver’ model?

Q.3. Under what circumstances would competition, or other procurement models such as open book contracting, have benefits over ex ante incentives as a cost control mechanism?

We think competition could be more advantageous than ex-ante regulation in a scenario where a central party dictates investment ahead of need. The primary benefits of competition that we have identified from our market activity includes cost and service benefits to customers, competitive pricing, and commercial accountability, as parties compete to be able to deliver the service. As IDNOs work with Independent Connection Providers in the distribution sector, we have also identified that risks associated with the build phase are reduced when inspection, monitoring, and adoption are carried out by other parties. This has the benefit of reducing regulatory cost of monitoring is principally delegated to network operators.

Q.4. What is your view on the options identified for simplification of incentive regulation? What would be the benefits and costs by comparison to the approaches used in RIIO-2?

A clear benefit of using Archetype 2, effectively an evolved version of the RIIO price controls, is the ability for quicker mobilisation as the structure is easier to understand and implement, given its current usage. Additionally, simplification of the existing framework provides continuing investor certainty. Conversely, there is an opportunity cost associated with ex-ante regulation and this would need to be managed at the highest level when setting targets.

Q.5. What are the network activities where there would be benefits for a move to an ex-post monitoring regime, and what would be the associated costs?

We think there may be benefits for network activities that are primarily considered business-as-usual (BAU) to be governed under an ex-post monitoring regime and a use case



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for this is the DCC. We do not think other activities would be appropriate (or even that archetype 3 is the most optimal approach for BAU activities) due to the considerations of ex post regulatory intervention which we have highlighted in our cover letter.

Q.6. What are the benefits and costs of this approach for Electricity Transmission by comparison to an evolution of the approach in RIIO-2, and what are the implementation barriers?

Where investment is mandated in advance and regionally optimised, the potential for a more agile and flexible electricity system are increased. A clear disadvantage of this approach is its ease and speed of implementation. It will require the FSO (or other centralised planner) to be operational well before the start of the next price control in order to be able to set strategic outputs following the close of ED-2.

Q.7. What is the potential for Electricity Distribution planning and commissioning to move to an alternative model by the end of RIIO-2, and what might be the benefits and costs of doing so?

We note that there are multiple hurdles involved with moving to an alternative model by the end of RIIO-2. Ofgem would need to establish the framework and methodology within the next two years. However, this poses a significant challenge as, depending on the archetype and building blocks selected, the FSO would need to be operational prior to implementation of the model and would ideally input into the framework and methodology.

One benefit of archetype 2 is that the framework and methodology have been established and would require only incremental change rather than wholesale reform to address the shortcomings identified in the strategic case for change.

Q.8. What is your view on the most effective approach to regulation of Gas Distribution and Transmission beyond RIIO-2? What would be the benefits and costs of moving to a simpler approach to regulation of the ongoing costs of operating and maintaining the network?

As the need for gas investment reduces in the coming years, a move to a less involved and simpler form of regulation that covers the ongoing costs of operating and maintaining gas networks would promote simplicity and certainty. Where this becomes a business-as-usual activity, the need for a detailed and robust monitoring regime also reduces, further reducing costs.



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Archetype 1 would appear to be the most appropriate approach to the strategic challenge of re-purposing the gas network.

Q.9. Should there be a shorter-term price control in gas distribution and/or gas transmission, and how could this work in practice?

We believe there should be an alignment with the electricity sector in order to maximise the value of the outputs of the FSO. Therefore, should archetype 1 be used more broadly, it would be prudent to have a shorter-term price control for Gas distribution and transmission to bridge the current gap.