
ADE Response | Ofgem consultation on the future of RIIO | 19 May 2023

Introduction

The ADE is the UK's leading decentralised energy advocate, focussed on creating a more cost effective, efficient and user-led energy system. The ADE has more than 160 members active across a range of technologies, they include both the providers and the users of energy equipment and services. Our members have particular expertise in heat networks, combined heat and power, demand side energy services including demand response and storage, and energy efficiency.

Response

Archetypes for future network regulation

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

The ADE's members, companies and communities investing and operating decentralised energy, constitute the scope of "consumers" for our points below.

A wide range of methods are currently used to collect and use customer feedback and priorities in the RIIO process. Further, in recent years, this has strengthened through the development of the Challenge Groups and the ESO's Performance Panel.

The ADE's experience is that the ESO's Performance Panel in particular has worked well. Whilst the level of additional revenue or penalties is relatively modest compared to the ESO's overall price control, the ESO has shown itself responsive to the Performance Panel's feedback and we consider it has created some positive changes.

The Challenge Groups have also been positive. The ADE has specifically participated in National Grid's Challenge Groups and found that the networks were responsive to feedback and that the relatively long-term nature of that group allowed expertise to develop amongst the challenge group which was positive and enhanced the level of scrutiny.

The working groups held to finalise the Output Delivery Incentives seem less effective. The issues are relatively complex and consultation has tended to come at a relatively late stage in the overall business planning process.

Finally, whilst high-level, the ADE does support Ofgem's consultative approach, particularly with respect to setting the framework for an upcoming price control. Further, whilst we welcome the transparency, the sheer size and detail of each business plan means that it is generally difficult for industry to offer effective feedback and challenge on the draft business plans.

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?

The ADE cannot comment on the overall view. However, we would like to raise the work currently underway to develop heat network zoning. The Energy Security Bill will provide powers to use these models to designate heat network zones in which heat networks, often far larger than we have seen in the UK to date, will develop and buildings will be mandated to connect. This will have a significant impact on both the local electricity and gas network infrastructure and may also impact the transmission infrastructure in this area.

This is likely to involve relatively detailed regional modelling, considering all buildings in a given area, their heat load and local sources of waste heat and this granularity should help inform the extent to which a detailed cross-vector view can be developed.

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?

The ADE does not have a view on this question.

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?

The ADE does not have a view on the overall costs and benefits of the approaches to simplification listed.

However, we would like to note that at present, the development and operation of flexibility markets may remain a function of a DNO licensed under such a new regime. If Ofgem returns to a RPI-X model for at least some areas, it is important that this does not disincentivise the networks' investment in flexibility markets where they are more cost-effective on a lifetime basis than capital investment. Further regarding this, the ESO's current price control and its cost pass-through approach for balancing services should offer some useful lessons for the development of such DSO functions at Distribution. This example notwithstanding, it is also important to note that benchmarking exercises may be of limited view with respect to distribution flexibility services because they are still relatively nascent and are likely to develop significantly in the coming years.

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?

The ADE supports the use of ex post-monitoring regime for the ESO through, for example, the Performance Panel, whilst noting that the extent of reward or penalties under the scope of that Panel is relatively small. Learning from this, we consider that this could be extended to the operation of flexibility markets at Distribution if this remains a function of the electricity distribution network licensees.

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?

The ADE does not have a comment on the overall benefits and costs. However, we would note that decentralised energy is facing very significant issues in securing connections, for both generation and demand, as a result of constraints on the transmission network. If the introduction of archetype 1 for new build allowed strategic, low regrets anticipatory investment to be built quicker than currently, this would be welcomed.

We would also note that the resulting framework for network charges for customers need to be considered at the same time as the models are considered. In particular, where a central body such as the FSO is directing strategic investment which may attract a different, and potentially higher, weighted average cost of capital in different areas of the country, a fair approach to the recovery of these charges needs to be considered. For example, it is unlikely to be fair for a regional population to recover the costs of a certain type of infrastructure that happens to be more expensive than that provided to another regional population. We consider that the implication of the move to models such as that presented for transmission is that network infrastructure cost across gas, electricity, hydrogen and heat networks needs to sit at a national, likely FSO level and be recovered from taxation, rather than a particular vector.

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?

Severe constraints are already being faced at Distribution. This, coupled with the introduction of regional heat network zoning in the early 2020s, means that strategic planning and investment in anticipatory investment at Distribution is needed this decade. This should be supported by the enhanced network monitoring being put in place across the distribution networks through RIIO-2.

In addition to this, distribution flexibility markets are likely to need to grow significantly this decade as more EVs, domestic heat pumps and heat pump-led heat networks are installed. The cost of not developing local markets to manage this increase in electricity load will be significant. Therefore, as with the infrastructure side, it is also important that the model for further developing flexibility markets is clear by 2028, whether this is part of the distribution networks, a future Regional System Operator and Planner or the FSO.

Finally, it is important that whatever model is chosen, there remains an overarching view on whether flexibility or reinforcement is the cost-effective option. This is now well-established and it is important that the imperative to build more quickly and ahead of need does not lead to the neglect of cost-effective alternatives.

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?

The ADE does not have a view on the overall costs and benefits.

However, we would raise that the approach to maintenance and decommissioning needs to include consideration of the introduction of heat network zones and the development of regional heat networks. This is important because the vast majority of connections to these heat networks, which may be upwards of 80-90% of buildings in a given regional zone, will replace the existing gas connection. If this needs considered carefully, it could lead to decommissioning parts of the gas network earlier than planned and therefore, higher costs than envisaged.

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

The ADE would support alignment of the price controls to 2028 to support whole system planning and the ability of the FSO to take and then direct investment across vectors.

Q.10. Would there need to be any changes to maintain a stable and consistent financial framework if we were to make greater use of different regulatory archetypes, and if so, what would those changes need to be?

The ADE does not have a view on the financial framework that will be needed to continue investment in the networks.

However, we would note that from a customer side, cost recovery on the basis of specific licensee as the shift to cross-vector planning and delivery develops does not seem sustainable. Increasingly, this could lead to customers in different regions contributing very differently as a result of strategic decisions made about which type of regional infrastructure can decarbonise their heating and industrial steam use most effectively. This will be based on local conditions, and not on factors that are within those consumers' ability to control either on investment or operational timescales. Further, moving all such costs onto electricity is not progressive and could hinder transport and heat electrification.

Q.11. Do you have any views on our proposed analytical approach?

No, the approach outlined seems reasonable.

For further information please contact:

Caroline Bragg

Director of Policy and Research

Association for Decentralised Energy

Caroline.bragg@theade.co.uk
