

Rebecca Barnett

Interim Director, Networks

Ofgem

By email: RegFinance@ofgem.gov.uk

Date

26 September 2023

Contact / Extension

Andrew Stanger

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Dear Rebecca,

Call For Input - Impact of high inflation on the network price control operation

SP Energy Networks (SPEN) represents the distribution licensees of SP Distribution plc (SPD) and SP Manweb plc (SPM) and the transmission licensee, SP Transmission plc (SPT). We own and operate the electricity distribution networks in South of Scotland (SPD) and North Wales (SPM), representing our customers on their behalf. We also own and maintain the electricity transmission network in South of Scotland (SPT).

With our ownership of these network assets, we are subject to the RIIO price control framework. The existing framework arrangements of providing a real return allowance using expected inflation, combined with the uplift of past investments (i.e. the RAV) by outturn inflation, have been consistent since privatisation. Investors value these arrangements and have made their long-term financing, investment decisions, and acceptance of final decisions on price control packages based on Ofgem's committed adherence to these inherent properties of the price control.

Certain policy intervention proposals considered by Ofgem in its Call for Input (CFI) have the potential to severely disrupt the long-established confidence that investors have in the stability and predictability of the GB regulatory regime, especially those in contrast to regulatory best practice i.e. retrospective adjustment. Undertaking an action that revises the outcome of past price controls (or re-opens current ones) would erode this trust and confidence¹, resulting in detriment to customers in the form of higher required returns from investors and reductions in resources directed towards service delivery and innovation.

It is our strongly held position that Ofgem should wholly dismiss any consideration of applying proposals on a retrospective basis (or reopening current price controls) as part of this consultation process. This sentiment is also borne by the investor community themselves, who are unanimous in their expectations on Ofgem to not proceed with implementing any such policy in this area given the significant detrimental effects that it would lead to.² The importance of ensuring Ofgem does not damage the attractiveness of

¹ See regulatory precedent extracts: ENA (September 2023), "Response to Ofgem Call For Input - Impact of high inflation on the network price control operation" p. 8-9

² See extracts from investor reports: ENA (September 2023), "Response to Ofgem Call For Input - Impact of high inflation on the network price control operation", p. 10

the sector to investors cannot be stressed enough in the current context of the additional investment in network infrastructure required to meet GB's Net Zero objectives.

It is important to put into context that the effect of any deviations between outturn inflation and ex-ante expectations will accrue in the RAV and be remunerated over a 45 year time horizon. Indeed, as a result of the existing regulatory arrangements the impact on nominal customer bills from the leverage effect, even over these unusual high inflationary years, has been shown by Ofgem in its CFI to not be material.³ It is clear that the damaging impacts from disrupting investors' trust and confidence in the regime, harming the sector's ability to raise the level of capital needed for Net Zero, would more than offsets any perceived benefit resulting from potential actions taken in this area to address the leverage effect.

It is wrong to characterise the recent variations between outturn inflation and ex ante assumptions as being inconsistent with Ofgem's policy intent. The extent of inflation exposure is company specific and based on their chosen financial risk management strategy. Investors have accepted and managed the inflation exposure based on their understanding of Ofgem's consistent policy position that financing decisions are best left to companies.⁴

We have repeatedly raised the point that companies' annual debt allowance does not cover the actual annual cash outflows for interest, and that shareholders are required to fund interest payments in excess of these allowances. Companies' actual debt performance in terms of net cashflow should be taken into consideration within this topic.

It is essential that any potential changes to regulatory arrangements are extensively assessed as part of the review on future price control frameworks only. We welcome working alongside Ofgem and relevant stakeholders to assess any policy options in detail to ensure they represent a net improvement over current arrangements if implemented in future frameworks. We are also open to working with Ofgem to assess options on how we can further clarify with stakeholders the comprehensive level of requirements already in place regarding dividends distributions as well as improving consistency in reporting practices.

In collaboration with the other Energy Network's Association (ENA) members, we have assisted in the development of the ENA's response to the CFI. We are fully supportive of the content and key messages expressed in this response. Our and the ENA's responses to the CFI are accompanied by the ENA commissioned report by Frontier Economics.⁵

Yours sincerely,

A handwritten signature in black ink, appearing to read "Scott Mathieson".

Scott Mathieson
Director – Network Planning & Regulation, SP Energy Networks

³ Ofgem estimates that the leverage effect to the end of FY 2022/23 has an average annual end customer bill impact of circa £2.30 assuming a 45 year payback period. See Ofgem (August 2023), "Call For Input Impact of high inflation on the network price control operation", p.5

⁴ "[W]e have long-held the position that network company financing decisions are for network companies and their shareholders and that they then bear the risks of these decisions." as stated in para 2.26 in Ofgem (May 2019), RIIO-2 Sector Specific Methodology Decision – Finance.

⁵ Frontier Economics (September 2023), "Comment on Ofgem's Call for Input on the effect of high inflation: A report prepared for the Energy Networks Association"

Have we characterised the issue accurately?

We agree with Ofgem's position in its CFI that differences between ex ante long-run expectations around inflation set at the beginning of the price control and outturn inflation will materialise over time. Network companies choose to accept the level of inflation exposure as part of their wider financial portfolio.

As Frontier Economics explain in their report accompanying the ENA response, in its decision to hold fixed coupon nominal debt, a network company takes on a "net inverse inflation exposure" which can result in the "leverage effect", where revenues from the indexation of the RAV exceed/fall short of the cost of nominal debt due to a mismatch between long-term inflation expectations and outturn inflation.⁶ The exposure is reduced through the holding of index-linked debt rather than fixed-coupon nominal debt.

However, it is a misconception that Ofgem's leverage effect is the consequence of a flaw in the regulatory policy setting of the notional company and one that is inconsistent with policy intent. We fail to see the basis of Ofgem's statement in its CFI that there is a "*key policy objective of keeping real equity returns stable relative to inflation over time*".⁷ Ofgem's footnote to this assertion in its CFI is misleading as the RIIO-ED2 FD makes no reference to this policy intention. Looking back at its setting of the RIIO-1 controls, Ofgem recognised that the cost of debt allowance mechanism exposes network companies to inflation risk.⁸ Exposure to variations around expectations are found across a multitude of mechanisms in the price control framework.

Network companies have borne the risk associated with inflation deviations across numerous price controls. There have always been slight disparities between forward-looking expectations and outturn inflation exhibited across time. Indeed, there have been periods where outturn inflation was lower than those assumed (i.e. went against equity investors) and Ofgem chose not to draw this issue to attention – indeed Ofgem's own analysis shows that during the RIIO-1 period (2013/14 to 2020/21) the ET and GD sectors experienced a cumulative loss due to the leverage effect.

We wish to highlight to Ofgem the technical clarification, as articulated by Frontier Economics in their report, that the leverage effect should not be viewed as a value transfer from customers to the company:

"Compared to issuing index-linked debt, where equity holders and debt holders are separately shielded from inflation risk, taking on nominal debt exposes both debt and equity holders to opposite sides of an inverse inflation risk. The inflation exposure of the equity investor is the leverage effect as described above in this paper, and by Ofgem in its CFI. The debt investor that purchases fixed coupon debt issued by the company takes on the other side of the exposure of the equity investor, i.e. the purchaser of a fixed rate debt product experiences a lower real return when inflation

⁶ Frontier Economics, (September 2023), "Comment on Ofgem's Call for Input on the Effect of High Inflation: A report prepared for the Energy Networks Association", para 63-64

⁷ As asserted in Ofgem, (August 2023), "Call For Input - Impact of high inflation on the network price control operation", p. 1.

⁸ Ofgem, (March 2011), "RIIO-T1/GD1 Strategy Decision – Financial Issues", para 3.55

is high and a higher real return when inflation is low. So when inflation is different than expected, there is no real terms impact on consumers, but there is a value transfer between the debt holders and the equity holders.⁹

To avoid any mischaracterisation going forward, the leverage effect should be represented as a transfer of value between the equity holders and the nominal debt holders during periods where outturn inflation deviates from the ex ante assumptions. Although equity and nominal debt investors' real returns are exposed to fluctuations due to differences between outturn and expected inflation, it should be clear that consumers do not face any real terms impact from these deviations. The effect should therefore not be viewed as a flaw in Ofgem's regulatory policy of indexation.

The exposure arises on a company actual basis based on the financing decisions taken. Ofgem's position has been that these decisions should be left to the companies and their shareholders themselves, who bear the risks associated with those decisions.¹⁰ Indeed, in the RIIO-2 review, Ofgem clarified that it would not be appropriate to share out-or-underperformance of debt costs with customers as the risk and additional intrusive regulation required from implementing such a policy would outweigh any potential benefits.¹¹

Have we adopted an appropriate approach to the quantitative assessment?

We consider that the methodological approach employed by Ofgem in its quantitative assessment of the leverage effect to be a reasonable one, albeit with minor modelling concerns identified and outlined by Frontier Economics in their accompanying report.¹² We would advise Ofgem to consider and address these concerns before any further potential policy consultation that is reliant on the quantification of the leverage effect is undertaken.

It is welcoming to see that Ofgem have made it clear in the CFI that the quantification of the leverage effect is highly dependent on the judgement made on several relevant factors within the assessment, all of which can significantly alter the quantum of the effect. Ofgem's recognition of these factors and the sensitivity on the overall estimated impact based on the methodological assumptions made (particularly around the length of the analysis period and the assumptions on forecast inflation) has come about following the ENA Finance Working Group and Frontier Economics' extensive collaborative engagement with Ofgem.

We also support the contextualisation of the impact in terms of customer bills. It is important to highlight how any outcome from regulatory arrangements impacts on customers, and how the operation of the existing regulatory arrangements of the energy network sectors (where the effect of lower/higher outturn inflation relative to ex-ante expectations accrue in the RAV and only realised over a 45 year time horizon) shows the illustrative customer bill impact of the leverage effect over the RIIO-1 period being small in nominal terms.

⁹ Frontier Economics, (September 2023), "Comment on Ofgem's Call for Input on the Effect of High Inflation: A report prepared for the Energy Networks Association", para 63

¹⁰ Ofgem, (May 2019), "RIIO-2 Sector Specific Methodology Decision – Finance", para 2.26

¹¹ Ofgem, (May 2019), "RIIO-2 Sector Specific Methodology Decision – Finance", paras 2.28-2.40

¹² Frontier Economics, (September 2023), "Comment on Ofgem's Call for Input on the Effect of High Inflation: A report prepared for the Energy Networks Association", Annex B

What are stakeholders' views on the policy options outlined and the associated benefits and risks associated with each option? Are there areas where the policy options outlined could be optimised? Please see the policy option section on page 7.

Option 1 – No policy action in relation to this issue

Option 1 to take no policy action is SPEN's preferred policy under consideration by Ofgem given the current regulatory arrangement's strong track record of delivering investment and ultimately benefits to the end customer. The current arrangements of long-term stable inflation-protected returns provided through an indexed RAV plus a real return, in combination with freedom for the network company to select the financial risk management strategy that best meets its needs, has been a cornerstone of network regulation since privatisation and it is one of the key reasons why a wide range of investors decide to provide large sums of their capital to energy networks, to the benefit of end consumers.

Ofgem's implementation and adherence to these regulatory policies and stable long-term expectations over time has established the strong degree of trust and confidence that investors' have in the stability and predictability of the regulatory regime. Investors and companies plan on the basis of these arrangements, including making long-term financing and investment decisions, and in their acceptance of final control decisions on price control packages.

The understanding that these long-standing arrangements would endure over the long-run has allowed companies' to build up their debt portfolios and financial risk strategies in an efficient manner, so as to benefit customers in the form of low financing costs and as a means to enable a vast quantum of investment and to dedicate resources towards innovative and cost efficiency measures which have led to significant advancements in service delivery and quality at a low and efficient cost to consumers.¹³

Under the current arrangements, the extent of inflation exposure is specific to the chosen financial risk management strategy chosen by a network company i.e. how much fixed coupon debt does it holds in its financial portfolio relative to index-linked debt (including derivatives), with the knowledge that deviations between outturn inflation and the long-run inflation forecast at the time of the price control will materialise. We would note that networks have been exposed to the leverage effect for decades, and equity investors who took on this exposure will have experienced lower effective returns during the RIIO-1 years up until the period to-date as a result of lower-than-expected outturn inflation.

We do not anticipate network companies to expect to receive higher or lower allowed returns over the long-run than that intended by Ofgem despite the existence of the leverage effect. Informed commentators do not see a reason to expect that outturn inflation to be systematically above or below the long-run inflation forecast used for setting the debt allowance over a long timeframe given the inflation target mandate set for the Bank of

¹³ See for example, Jamasb T., & Pollitt, M. (2007), "Incentive regulation of electricity distribution networks: Lessons of experience from Britain. *Energy Policy*", 35(12), 6163-6187

England and its strong contractionary monetary policy decisions to date. Any decision by Ofgem should be fully reflective of this long-term expectation.

Regardless, it is important to put into context that any advantage or disadvantage from the net financing exposure would accrue in the RAV and transfer through as reductions or increases to revenues (and hence customer bills) over the long-term (45 years) – the impact on customer bills in nominal terms from the leverage effect, even over these unusual high inflationary years, has been shown by Ofgem in its CFI to be relatively small.

On the other hand, a significant change to these long-standing arrangements has the potential to disrupt the established strong investor confidence in the sector and alter their perception of the risks involved with investing in the sector, potentially increasing the long-term cost of capital. Companies would also have to react and rebalance their portfolios based on any changes, potential incurring additional costs and increasing financial resilience risks.

The current arrangements have helped establish and strengthen the strong investor appetite in the sector, which has ensured the delivery of the observed large scale of investment. This capital has enabled the crucial expansion and enhancement of the network to meet evolving needs, and that it has been financed at a low and efficient cost to customers over time. Any changes to these regulatory arrangements must be weighed against the clear benefits that they have been delivered to customers over the long-term.

The risks associated with upending these demonstrable beneficial long-standing arrangements cannot be underestimated: it could risk destabilising the credibility of the regulatory framework, damaging investor trust and confidence in the predictability and stability of the GB regime at a time when the sector needs to retain attractiveness to investors in order to achieve the significant additional investment required to deliver on the Government's Net Zero objectives.

Option 2 – Distribution policy reporting and transparency

Network companies operate under a robust regulatory framework established by Ofgem regarding dividends and the reporting of regulatory financial information. The framework encompasses a comprehensive set of financial obligations and mechanisms that have been designed to effectively manage the appropriate financing of network companies.

We would emphasise that a noteworthy aspect of the existing arrangements is the emphasis on companies to evidence financial resilience. Under our licence arrangements, we are subject to various financial resilience reporting obligations. We approach these obligations with the utmost seriousness and commitment. The ENA's response to the CFI provides an extensive list of the various financial obligations in place under the RIIO-2 frameworks.¹⁴

¹⁴ ENA, (September 2023), "Response to Ofgem Call For Input - Impact of high inflation on the network price control operation", Appendix 1

Specifically, regarding dividends, Ofgem has already established extensive requirements on the reporting of dividend policies and dividend distribution. We are required to report substantial financial detail under the Regulatory Financial Performance Reporting (RFPR) requirements. The RFPR provides customers and stakeholders with a comprehensive, transparent, and accurate measure of network company financial performance under the current price control framework.

It is important to note that Ofgem already maintains a large degree of authority to investigate and, when deemed appropriate, take any necessary enforcement actions if it identifies any failure from networks in meeting these obligations. This ensures accountability and compliance within the industry.

We do, however, acknowledge that there may be a lack of public clarity on the extent of requirements we are subject to as well as the challenges for stakeholders and customers to fully comprehend the rationale behind our, and other networks', decisions around the timing and level of dividend distributions given the intricacies and complexities inherent in the regulatory framework e.g. dividends may be linked to long-term financing needs, and there is often a disparity between the timing of cash-flows and the actual performance linked to those cash-flows.

We are open to working with Ofgem to assess options on how we can further clarify the comprehensive level of requirements already in place regarding dividends, with the goal of enhancing transparency for stakeholders around our dividend distribution decisions and how they link to our performance under the price control, as well as consistency in our reporting practices.

Option 3 – Changes to future price control design

As highlighted in our response to Option 4 below, we would further stress the importance of restricting any application of changes to the regulatory framework to future price controls only given the detrimental effects the opposite approach (i.e. reopening historic and/or current price controls) would have on investors' trust and confidence in the regulatory regime, and their appetite for investing in the sector.

In relation to the various sub-options suggested by Ofgem in its consideration of potential changes to the design of future price controls to address the leverage effect, we would point to the observations outlined by Frontier Economics in respect to these proposals in section 3.2 of their report.

Importantly, as Ofgem themselves acknowledge, we are in the very early stages of the consultation process regarding this topic. It is therefore not possible to explore or analyse the various sub-options as set out in the CFI in sufficient detail or assess how they compare relative to the existing arrangements given the high-level presentation and lack of detail provided for each option. Any assessment of design options surrounding such a topic that comprises a high degree of complexity as well as interlinkages with other aspects of the price control package needs to be undertaken on a thorough and extensive basis, requiring

further information and a full impact assessment from Ofgem on the exact design of these methodology changes.

To summarise, the non-exhaustive list below highlights the high-level views set out by Frontier Economics (which we agree with) on the potential consequences that may come about from the adoption of the listed methodology design changes:

- Fundamentally altering price control mechanics and the basis on which the cost of capital is set
 - Proposed changes could reduce inflation protection on past and future investments, reducing investor appetite in the sector.
 - Some options may result in different rates of return for companies, based on financing choices rather than inherent differences.
 - Regime may transition from a notional company basis to an actual company approach, overturning the long-standing position on financial structure flexibility.
- Risk of unintended or detrimental consequences
 - Increased revenue volatility relative to current arrangements due to necessary revenue adjustments. Changes to timing and speed of cash-flows, potentially over the short-term.
 - Alteration of rating agencies appraisal approach to network companies, impacting their debt costs.
- Create practical complexities and additional regulatory burden in implementation
 - Additional complexity in setting of the WACC allowances due to inclusion of nominal components – impacts on NPV neutrality of revenue exercises.
 - Potential for extensive RAV segmentation, which would require differing indexation.
- Lack of clarity on whether leverage effect can be fully eliminated due to companies' selecting financing choices that deviate from the notional assumptions used in Ofgem's calibration of the selected methodology option.

Regardless, the assessment of any new mechanism needs to be clearly evidenced by all relevant parties and carefully assessed over an extensive consultation process to see how it compares relative to the existing regulatory arrangements. Given the interlinkages with other aspects of the price control framework, any methodological changes would need to be robustly assessed by considering the entirety of the financial arrangements in the package given the protections offered to both network companies and consumers. We would strongly suggest that any such work be undertaken as part of the upcoming price review process, with the Sector Specific Methodology Consultation being the earliest feasible area where this work could begin to take shape.

SPEN welcomes future engagement with Ofgem to ensure that any changes considered to the framework in relation to this topic for the next set of price controls are assessed in a robust and sufficient manner, and to establish if they are indeed in customers' best short- and long-term interests relative to the current arrangements.

Option 4 – Out or underperformance true up

SPEN are unambiguously opposed to this policy intervention option since, as Ofgem themselves acknowledge, it would materially damage investor confidence in the stability and predictability of the regulatory model applicable to GB energy networks, creating significant costs for present and future consumers due to investors elevated levels of perceived regulatory risk in the regime. The option should be disregarded as a considered policy intervention going forward to avoid any further concern from investors regarding their confidence in the arrangements of the regime.

As outlined in detail by Frontier Economics in section 2.2 of their report, a retrospective adjustment or clawback is clearly not in the interest of customers due to the highly detrimental effects that would arise from such an action, such as a sustained increase in investors' required cost of capital (ultimately borne by customers) due to the perception of elevated regulatory risk, and reduction in resources allocated towards innovative and cost efficiency measures.

Applying an ex post clawback of part of the RAV indexation that has occurred would signal to investors that returns legitimately earned under an already agreed upon regulatory framework will now have the potential of being expropriated by the regulator if deemed to be above a perceived 'appropriate' level. This would not only increase investors' required rate of return due to their elevated perception of regulatory risk in the sector, but it would also negatively impact on their commitment levels to investments related to innovation delivery and service quality improvements as they will now see outperformance related to other elements of the regulatory framework at risk of being appropriated by Ofgem – increasing costs and undermining the incentives to improve service delivery and innovate is clearly not in consumers interest.

Crucially, the damage caused to the overall stability and confidence in the regulatory regime would lessen the overall investment attractiveness of the industry at a time when the sector faces increased competition for vital capital required to finance the significant scale of additional investment needed to deliver on the country's Net Zero and energy security ambitions.

Imposing such fundamental retrospective changes to regulatory arrangements on a reactive and unexpected basis and the associated detrimental effects to consumer interests has been recognised by both the CMA and Ofgem, as evidenced in detail in Frontier Economics' report.^{15,16}

Investor analysts and rating agencies themselves have clearly indicated that they do not consider a policy of retrospective action to even be pursued by Ofgem given the clear detrimental effects that it would have on the credibility of the regulatory framework, thereby

¹⁵ Frontier Economics, (September 2023), "Comment on Ofgem's Call for Input on the Effect of High Inflation: A report prepared for the Energy Networks Association", Section 2.3

¹⁶ Frontier Economics, (September 2023), "Comment on Ofgem's Call for Input on the Effect of High Inflation: A report prepared for the Energy Networks Association", Annex A

damaging investor confidence in the stability and predictability of the regulatory regime.¹⁷ The investor community are clear that employing such a policy intervention would ultimately lead to lower levels of investment in the sector and increasing costs unnecessarily to current and future consumers.

The rejection of this policy intervention not only applies to historic price controls, but also to the price controls currently under operation (i.e. RIIO-2). Network companies and their investors have established debt portfolios and financial risk strategies based on the confirmed policies and expectations set at the determination of the price control package. Applying such a change to the current framework would constitute a re-opening of a price control – even if only applied to the remaining future years of a price control – and would impose an entirely different financial and regulatory risk on investors than those signalled to them at the time of the determination of the regulatory package. Companies would have to react and rebalance their portfolios, incurring additional financing costs at a time when such costs have materially increased.

Option 5 – Voluntary submissions by licensees

We do not consider this option of voluntary contributions from licensees to be an appropriate policy intervention in respect to this area. An integral part of the regulatory framework is that network companies are allowed to freely select the financing policy that best suits their long-term investment needs and aims, part of which includes selecting the level of inflation risk it is willing to be exposed to.

The expectation that networks companies should voluntarily return the perceived benefits accrued when outturn inflation exceeds ex ante assumptions, whilst at the same time fully bearing the risk and any disbenefit under the opposite scenario (as was the case over much of the RIIO-1 period) is unfair and is ultimately akin to a form of retrospective adjustment.

An intervention of this type would ultimately lead to the same detrimental effects on investor confidence and customer interest as outlined in our response to Option 4 above. In the context of ensuring the industry's attractiveness to investors to ensure provision of the necessary capital to finance the required step up in investment designed to meet the country's Net Zero targets, it should not be a policy intervention option that Ofgem should pursue any further in respect to addressing any concern regarding this topic.

Should any other policy options be considered? / Is there any further information or are there other factors which should be considered?

At this early stage we do not consider there to be any further policy intervention options that should be highlighted or explored further within this area primarily due to the long-established success of the current regulatory arrangements. If Ofgem were to decide to consider additional policy options, due to this expected short-term issue, then we would

¹⁷ See extracts from investor reports: ENA (September 2023), "Response to Ofgem Call For Input - Impact of high inflation on the network price control operation", p. 10

propose Ofgem follow appropriate regulatory best practice when informing and consulting with stakeholders on its proposals.

We believe stakeholders continue to display a fundamental knowledge gap on the actual debt cashflow position on network companies' embedded debt each year. There is a lack of understanding that companies' annual debt allowance provided through the RIIO framework does not cover the actual annual cash outflows for interest. Ofgem's arrangements for the long-term collection of returns (remunerated over 45 years through interest and depreciation on the RAV) is set to incentivise long-term responsible investment and stability in the networks. However, the policy leads to a short-term negative cashflow position, which is then required to be funded by shareholders.¹⁸

We propose that any future assessment should take into account companies' actual debt performance in terms of net cashflow.

Are the principles proposed for policy formulation complete and appropriate? / Do the proposed evaluation criteria comprehensively consider the consumer interest in respect of this issue? Are there modifications or additional criteria that stakeholders would suggest?

We consider the policy formulations listed by Ofgem to be appropriate and we support these being adhered to throughout the anticipated programme of work of exploring and in the assessment of any potential future policy intervention.

We would highlight to Ofgem that the proposed set of criteria listed in the CFI used when evaluating policy options should be extended to consider how any future changes to the design of the regulatory framework impacts on other aspects of the price control, as well as considering more holistic aspects of the price control.

As outlined in the ENA's response,¹⁹ we recommend that Ofgem should consider the consequential implications on other areas of the price control from any policy action, which could include the consideration on areas, such as NPV calculations supporting investment appraisals and revenue timing adjustments.

In addition, the additional holistic assessment criteria that Ofgem should include in its assessment should cover:

- Impact on customer bills – including inter-generational differences and stability of network charges;
- Implications for incentive properties and incentive strength; and
- Impact on investability of the framework and its ability to compete for finance in global markets.

¹⁸ Further detail can be found in our RFPR submissions. Accessed here: https://www.spenergynetworks.co.uk/pages/regulatory_financial_performance_report.aspx

¹⁹ ENA (September 2023), "Response to Ofgem Call For Input - Impact of high inflation on the network price control operation", p. 14

We also recommend that Ofgem consider whether any transitional arrangements should be put in place to minimise/eliminate any adverse effects from any policy change.

We agree with Ofgem's assessment in the CFI that there is a need to proceed very carefully on this issue. Overall, if Ofgem should decide to proceed, it must approach the evaluation of any proposed policy option with a great degree of consideration and appropriate assessment in order to robustly conclude whether a policy change represents a clear and evident net improvement to the overall design of the price control framework over the current regulatory arrangements. This would ensure that any changes made to the framework going forward are ultimately in customers best interest and avoid any adverse unintended consequential changes to other aspects of the price control framework.