

The background of the slide features a large, semi-transparent white arrow pointing from the bottom-left towards the top-right. The background is a composite image with a blue-toned left side showing a perspective view of a modern building or infrastructure, and a right side with a warm-toned image of a large, multi-layered turbine or engine component. The overall aesthetic is clean and professional, with a focus on energy and infrastructure.

RPI-X@20: Emerging Thinking

Delivering value for money in the longer term

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Areas for discussion

Longer term efficiency

- Encouraging a focus on best value solutions over the long term

Length of the price control

Incentives for efficient delivery,

- augmented by:
- an innovation stimulus
 - a greater role for competition

Overview of proposals included in Emerging Thinking

Opportunity for discussion of these issues and to hear your views

Encouraging value for money over the longer term

Set out package of ideas focused on encouraging delivery at value for money over the longer term under an outcomes-led framework:

Re-focused incentives on output delivery, value for money over the long term, working with others, and responding to and anticipating future needs

Innovation
stimulus

Competition in
delivery and
tendering

Options for lengthening elements of
the control

Proportionate and differential treatment of networks, reflecting track record for planning/delivery

New business plan requirements would complement these ideas

- The proposed new framework would also encourage networks to consider interactions between the price control and charging
- We set out ideas on options for providing rewards and downsides: explicit rewards, allowed revenue adjustments, and potential constraints on recovery

Length of the price control

Options on duration of price control to encourage longer-term perspective

Five-year controls with longer-term focus

- Retain five-year price control duration
- Company business plans set in long-term context
- Supported by innovation stimulus

Extend price control period (e.g. ten years)

- Outputs and revenues fixed for longer period
- Company has greater stake in long-term costs
- Concerns about flexibility and forecasting risks

Partial longer-term price controls

- Longer-term price controls with partial review of specific areas planned mid-period (e.g. outputs)
- Network has financial stake in longer-term costs
- Reduces risks from full extension of period

A greater role for competition in delivery

Tendering certain aspects of output delivery could deliver benefits through strengthening incentives or facilitating third party involvement:

Expose actual
efficient costs

Delivery of quality,
innovative solutions
at value for money

Present opportunities
for mitigating/
diversifying risks

Merit in establishing tendering as part of the regulatory 'toolkit' to drive efficiency where this does not jeopardise timely delivery

- Questions of "whether and how" would be considered on a case-by-case basis, supported by published guideline principles on use of tendering
- We envisage that most aspects of network services will continue to be delivered by existing networks

We also intend to explore use of our ability to revoke network licences and then franchising as potential way forward

A specific innovation stimulus

An outputs focused regime with appropriately designed incentives and enhanced competitive pressures should encourage networks to innovate to deliver defined outputs effectively

Barriers to innovation to facilitate a sustainable energy sector

Benefits may accrue to a range of parties

Potentially significant upfront costs

Long term private cost to networks of not innovating may not be significant

Networks do not face a significant carbon price

In the interim a cross-sectoral, time limited innovation stimulus open to a range of parties may be needed

➤ Stimulus would build on the Low Carbon Networks Fund

➤ **Would be introduced at the next round of price reviews for transmission and gas distribution**

➤ **Electricity DNOs have the opportunity to obtain funding through the LCNF**

Questions

1. What aspects of this package do you think are best placed to encourage delivery of value for money in the longer term?
 2. Do you think that financial commitments for longer than five years for some elements of the price control might facilitate efficient longer term delivery?
 3. Do you have any views on our ideas for how interactions between charging and price review incentives might be taken into account at price reviews?
 4. In what circumstances do you see tendering contributing to delivery at value for money in the longer term?
5. What role do you see an innovation stimulus playing in encouraging delivery at value for money in the longer term?

Are there other areas you would like to cover?

The logo for ofgem, consisting of the word "ofgem" in a white, lowercase, sans-serif font, centered within an orange rounded rectangle. The background of the slide features a collage of images: solar panels on the left, a large white arrow pointing right, and a close-up of a gas meter on the right.

ofgem

Promoting choice and value
for all gas and electricity customers