

RPI-X@20 consultation - Local Grids and RPI-X@20
Ofgem
2nd floor
9 Millbank
London
SW1P 3GE

RPI-X20@ofgem.gov.uk

Dear Cloda,

RPI-X@20 – Emerging thinking

The Renewable Energy Association is pleased to be able to comment on this landmark document. As you are aware our members work on all types of renewable power and heat projects connected at both transmission and distribution levels in all parts of Great Britain. Our members are also involved with injection of biogas into the gas network and heat distribution networks. Whilst we are therefore primarily interested in the regulation of electricity transmission and distribution networks we are also concerned with gas networks and potentially any emerging heat distribution networks.

We are generally supportive of re-examining the fundamentals of network regulation after 20 years of the RPI-X methodology. However, what emerges may not in fact be very different in practice from the sort of price control settlements reached recently. These have become quite complex and a long way away from the original basic RPI-X philosophy. The latest settlements, to some degree, have been designed to give incentives to deliver specific outcomes. It is a natural progression from there to a regulatory regime based on achieving particular outcomes. The risk in becoming too prescriptive in what outcomes the regulated company is being asked to achieve is that regulation will turn into de facto micromanagement of the network companies.

Specific questions

Chapter 1

Question 1: Do you think our desired outcomes for the future regulatory framework are appropriate? Are there any we have missed?

We think that you have expressed the outcomes sufficiently broadly to capture all the desired outcomes. We particularly welcome the emphasis given to playing a full role in facilitating a sustainable energy sector.

Question 2: Do you agree that we need a fundamental change to the existing 'RPI-X' frameworks to ensure these outcomes are delivered?

Whilst a fundamental change from the basic vanilla RPI-X approach is needed it is recognised that the most recent settlements have actually been more complex, than that involving a number of different incentive schemes each associated with delivering a particular outcome or behaviour. What is suggested in this document may not therefore be very different in practice from a formalisation of what the RPI-X form of regulation has already in practice evolved into.

Question 3: Do you think the suggested new framework is the best way of delivering these outcomes in the future? Are there any aspects you would change? Have we missed any key aspects?

In general, yes. In practice the difficult issues in implementing the approach will be to get the right balance between defining the outcomes in sufficient detail and micromanaging the companies, and also setting appropriate time periods over which each aspect of the price control arrangement is to last.

Chapter 2

Question 1: Do you agree that a new regulatory framework should focus on delivery of desired outcomes?

Yes, after all "desired outcomes" are what the users of networks or indeed any product or service want. Clearly they want these outcomes at the lowest possible cost, which is achieved in a regulated environment by balancing the strength of the incentive arrangements against the consequences of increased company riskiness on the cost of raising funds.

Question 2: Do you have any comments on the categories of outputs related to these outcomes?

There is no category related to asset health. The end result of poor asset health is unreliability, once this has begun to manifest itself it may be too late to rectify at a reasonable cost. Some sort of measure related to asset age for example may be appropriate.

Question 3: Do you have any comments on how these outputs should be incorporated into the new regulatory framework?

We agree that output measures should generally be proposed by companies following discussion with stakeholders and then agreed with Ofgem. On occasion it may be appropriate for Ofgem itself to propose output measures.

Chapter 3

Question 1: Do you agree that it is appropriate for network companies and Ofgem to improve their engagement with stakeholders as a way of improving the quality and legitimacy of decision making? Do you have any ideas on how to improve engagement by network companies and Ofgem?

In general, it is a good idea to engage with those, who are impacted by price control decisions, in the process as much as possible. We recognise that often such parties do not have the time or resource to participate as much as would be ideal, but we see little alternative to making as many opportunities available as possible. There are both advantages and disadvantages of meetings / workshops and consultation processes where parties are invited to submit written views, whether conducted by Ofgem or the network companies. A mixture of both is needed to maximise stakeholder participation.

Question 2: Do you think we should consider introducing a third-party merits-based right to challenge our final price control proposals?

Yes, but the timing of such challenges would have to be carefully proscribed to avoid inserting an additional period in the price control process.

Chapter 4

Question 1: Do you have views on our suggestion that financial commitments could be provided for longer than five years for some elements of the price control? What would be the appropriate length of this partial „longer“ period? To which aspects of the control might it be appropriate to give a longer-term commitment?

It is entirely appropriate that financial commitments should in some cases be for longer than five years, particularly those related to investments in an asset with a long life. In practice to some extent rolling over asset values into the next price control period is already a form of extending the period. Different desired outcomes and incentive mechanisms for them may require different periods of validity and these should be set individually.

Question 2: Do you have views on our suggestions on what business plans might look like in the new regulatory framework?

One item to be considered is to what extent the regulatory business plan could be combined with information reporting. In view of the probable

overlapping timescales of different outcome targets it is likely that the regulatory plan will be kept updated on a rolling basis annually, without of course losing track of targets that have been agreed to cover longer periods.

Question 3: Do you have comments on our ideas on how efficient costs might be assessed in the new regulatory framework?

There is little alternative to the use of experts and benchmarking against other companies.

Question 4: Do you have comments on our ideas on how efficient long-term delivery might be incentivised in the new regulatory framework?

We agree it is important that there is no regulatory incentive to achieve an outcome via one route rather than another because of unequal incentive rates.

Question 5: Do you have comments on our suggestions of how the new regulatory framework might encourage network companies to anticipate and deliver on the needs of existing and future consumers and network users?

Clearly there is scope for giving additional returns for investment in which there is additional risk. It may be appropriate to let the network companies themselves select from a risk / reward menu for certain types of expenditure.

There is also scope to use industry consensus building about what is needed in some circumstances. An recent example of this is the ENSG transmission for 2020 process.

Question 6: Do you have views on our ideas on how the interactions between charging and price review incentives might be taken into account at price reviews?

In general we feel that charging arrangements have their own statutory and license requirements, and compliance with these should be enforced. We do not think that in general it is helpful to give network companies financial incentives to adopt a particular pricing structure rather than another one. It should be a matter of license etc. compliance.

Question 7: Do you have comments on our suggestion to treat companies differently at the price control, both in terms of process and incentives, reflecting planning and delivery performance?

Any differences between companies in the same business need to be justified on a case by case basis.

Question 8: Do you have views on our suggestion to open up some aspects of delivery to competition? Office of Gas and Electricity Markets 48 Emerging Thinking consultation document January 2010 Appendices

Appropriate competition should be encouraged but it should not be encouraged in situations to fragment responsibilities in situations where it is more efficient to have a single party responsible for a complete area of delivery.

Question 9: Do you have comments on the design of a cross-sectoral time-limited innovation stimulus that is open to a range of parties?

A fund modelled on the low carbon networks fund would be an appropriate way forward.

Question 10: Do you have comments on our straw man on how we would embed our financeability duty into the new regulatory framework?

No.

Chapter 5

Question 1: Do you agree that a new regulatory framework can deliver our desired outcomes within the existing industry structure?

Yes. There may be arguments for altering the industry structure in some areas but these are not in the main related to the difficulty of providing appropriate regulation.

Question 2: Do you agree that it is appropriate to encourage network companies to work with others to identify cross-sectoral solutions to the challenges the sector faces?

Yes, in general the network companies are not in competition with each other. There should be no barriers to cooperation and sharing good ideas on best practice as well as joint programs to develop new techniques.

Question 3: Do you agree that the regulatory framework should ensure energy network companies facilitate effective competition in energy services?

Yes, although it is not at present clear what sort of activities energy service companies might perform that would not fall into the category of either supply (including all the activities for which the supplier is responsible for) or IDNO operation and would require an interface with a network company.

We hope you find these comments useful. If you would like to discuss them further please feel free to get in touch.

Yours sincerely

Gaynor Hartnell
Director of Policy