

## Glossary of terms: RPI-X@20 review

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### A

#### Active distribution network

The function of an active distribution network is to efficiently link power sources with consumer demands, allowing both to decide how best to operate in real time.

#### Administrative burden

Things that business must do or other administrative costs that businesses sustain due to a requirement from regulation. This may include keeping records or responding to information requests<sup>1</sup>.

#### Agency for the Cooperation of Energy Regulators (ACER)

The agency responsible for coordinating national regulatory authorities in Europe. ACER also participates in the creation of network rules, takes binding decisions on cross border energy infrastructure and provides advice on various energy related issues to the European institutions.

#### Allowed revenue

The amount of money that a network company can earn on its regulated business.

#### Areas of Outstanding Natural Beauty (AONB)

Areas which are protected by legislation due to their visual or environmental qualities. Electricity networks are provided with an allowance for the undergrounding of cables in these areas.

#### Asset stranding

Assets which have subsequently become either not used or under-used as compared with initial expectations.

#### The Authority/ Ofgem

Ofgem is the Office of Gas and Electricity Markets, which supports the Gas and Electricity Markets Authority (GEMA), the body established by section 1 of the Utilities Act 2000 to regulate the gas and electricity markets in Great Britain.

### B

#### Baseline capacity

Baselines define the reference levels of capacity that the transmission licensee is to release. Baselines also determine the level above (or below) which incremental capacity is defined.

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<sup>1</sup> <http://www.berr.gov.uk/whatwedo/bre/policy/simplifying-existing-regulation/administrative-burdens/page44061.html>

## Baseline capital expenditure

Baseline capital expenditure is the total amount of capital expenditure set up front at the price control review. It includes both load related Capex and non-load related Capex.

## Base revenue

Base revenue is the amount of revenue network companies are allowed to recover as set up front at the price control review. Additional revenue may be allowed during the review under certain, specified circumstances, for example, if it becomes apparent that additional expenditure is required due to greater demand than predicted.

## Benchmarking

The process used to compare a company's performance (e.g. its costs) to that of best practice or to average levels within the sector.

## Better regulation and better regulation principles

Established principles of better regulation state that regulation should be transparent, accountable, proportionate, consistent, and targeted only at cases where action is required.

Ofgem has interpreted better regulation to mean only regulating where necessary whilst designing rules that support competition and protect the customer. As part of our better regulation work Ofgem develops an annual Simplification Plan to help reduce the burden of administration while ensuring consumer protection<sup>2</sup>.

## Bilateral contracts

Two sided contracts which contain terms of reference to both parties involved and to which they are bound.

## Biogas

A gas produced by the biological breakdown of organic matter in the absence of oxygen. This gas can be used in a similar manner to natural gas to produce heat or electricity but unlike natural gas, biogas is a renewable fuel.

## Bond

A type of debt instrument used by companies and governments to finance their activities. Issuers of bonds usually pay regular cash flow payments (coupons) to bond holders at a pre-specified interest rate and for a fixed period of time.

## British Electricity Trading and Transmission Arrangements (BETTA)

BETTA introduced a single GB-wide set of arrangements for trading energy and for access to and use of the transmission system.

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<sup>2</sup> Further details can be found at the following link:  
<http://www.ofgem.gov.uk/About%20us/BetterReg/Pages/BetterReg.aspx>

## Building blocks approach

Building block reviews focus on determining appropriate values for each company's own capital asset values, weighted average cost of capital (WACC), capital expenditures and operating expenditures for the upcoming price control period.

## Department of Business, Innovation and Skills (BIS)

### Business plans

The company's forward looking expenditure plans/expectations which are submitted to Ofgem as part of the price control review process.

### Business support costs

Business support costs are related to functions that are not core to provision of network services but that are required for the smooth running of the business. These are likely to include costs associated with finance department, human resources, and central IT systems.

## C

### Capacity (gas)

The amount of natural gas that can be produced, transported, stored, distributed or utilised in a given period of time under network design conditions.

### Capital Asset Pricing Model (CAPM)

A theoretical model that describes the relationship between risk and required return of financial securities. CAPM states that the expected premium ( $r$ ) on any security equals its beta ( $\beta$ ) times the market risk premium (market return ( $r_m$ ) minus the risk free rate ( $r_f$ )).  $r = r_f + \beta(r_m - r_f)$ .

The basic idea behind the CAPM is that investors require a return for the rate of interest, and a return for the level of risk in their investment.

### Capital expenditure (Capex)

Expenditure on investment in long-lived network assets, such as underground cables, overhead electricity lines and substations.

### Capital structure

(See financial structure)

### Capitalisation policy

The approach that the regulator follows in deciding the percentage of total expenditure added to the RAV (and thus remunerated over time) and the percentage of expenditure remunerated in the year it is incurred.

### Carbon Capture and Storage (CCS)

Carbon capture and storage (CCS) is a three stage process involving (1) capturing CO<sub>2</sub> emissions from power stations or other industrial sources; (2) transporting the CO<sub>2</sub>,

usually by pipelines, to storage points; and (3) storing it safely (e.g. in depleted oil and gas fields).

### Carbon Emissions Reduction Target (CERT)

The CERT programme replaced the Energy Efficiency Commitment 2005-2008 as the government's domestic efficiency obligation on energy suppliers. It sets an obligation on energy suppliers to reduce CO<sub>2</sub> emissions by promoting energy efficiency and micro renewables to domestic energy users.

### Carbon footprint

Total amount of greenhouse gas emission caused directly and indirectly by a business or activity.

### Carbon price

A carbon price is a term for a value applied to each unit of carbon emissions. A carbon price can be set by differing methods, such as by the social cost of carbon.

### Claw back

When a company makes large savings due to spending far less than the revenue that was set at the price control, the regulator may decide to take some of this revenue back 'ex post' i.e. retrospectively and pass some of the savings onto consumers. This is known as a claw back.

### Cliff edge (depreciation)

As part of DPCR3 and DPCR4, asset lives were reduced from 33 years to 20 years with the difference smoothed over a 15 year period. This accelerated depreciation is known as cliff edge depreciation.

### Combined heat and power (CHP)

The simultaneous generation of usable heat and power (usually electricity) in a single process, thereby leading to reductions in the amount of wasted heat.

### Community Energy Savings Plan (CESP)

A government programme targeted at low income communities in around 50 - 100 areas, offering free and discounted central heating, energy efficiency measures and small scale generation projects.

### The Competition Commission (CC)

An independent public body which conducts in depth inquiries into mergers, markets and aspects of regulation of the major regulated industries.

### Consumer

In considering consumers in the regulatory framework we consider users of network services (for example generators, shippers) as well as domestic and business end consumers, and their representatives.

## Consumer Prices Index (CPI)

The CPI is an aggregate measure of changes in the cost of living in the UK. It differs from the RPI in that, it does not measure changes in housing costs and mortgage interest repayments - whereas the RPI does, they are calculated using different formulae, and have a number of other more subtle differences.

## Connection and Use of System Code (CUSC)

A multi-party document creating contractual obligations among and between users of the GB transmission system, parties connected to the GB transmission system and national grid, in relation to their connection to and use of the transmission system.

## Constructive engagement

Process whereby different parties are given the opportunity to reach an agreement on a number of price control related issues, with the regulator acting as a facilitator.

## Consumer Challenge Group

The Consumer Challenge Group was set up to ensure that the consumer view was fully considered during the 2010-2015 Electricity Distribution Price Control Review. The Group of six consumer experts acted as Ofgem's 'critical friend' and brought additional expertise that Ofgem could not address through market research.

## Consumer First Panel

The Panel, set up by Ofgem, consists of 100 domestic customers, recruited from five locations across Great Britain. The Panel meets at least three times a year to discuss key issues related to energy. It was first established in July 2008.

## Contracting out

A business relationship, where the contracting body grants responsibility for the provision of a good, service, or activity to an external organisation.

## Corporation tax

A UK tax levied on a company's profits.

## Cost driver

A cost driver is any factor which alters the cost of an activity.

## Cost of capital

This is the minimum acceptable rate of return on capital investment. It includes both the cost of debt to a firm, and the cost of equity.

## Customer interruptions (CIs)

The number of customers in every 100, whose supplies have been interrupted per year over all incidents, where an interruption of supply lasts for three minutes or longer, excluding re-interruptions to the supply of customers previously interrupted during the same incident.

## Customer minutes lost (CMLs)

The duration of interruptions to supply per year – average customer minutes lost per customer per year, where an interruption of supply to customer(s) lasts for three minutes or longer.

## D

### Demand side management (DSM)

Demand side management (or load management) is any mechanism (both social and mechanical) that allows a customer's demand to be intelligently managed in response to events on the power system. Such events would include lack of network capacity or insufficient generation.

### Depreciation

Depreciation is a measure of the consumption, use or wearing out of an asset over the period of its economic life.

### Discretionary adjustments

Adjustments made to the revenue of a network company at the discretion of the regulator. For example, adjustments may be used to reward both good and bad performance in a particular field not allowed for by another mechanism.

### Discretionary reward scheme (DRS)

An Ofgem run scheme designed to financially reward DNOs and GDNs for better performance in areas that cannot be easily measured or incentivised.

### Distributed generation (DG)

Any generation which is connected directly to the local distribution network, as opposed to the transmission network, as well as combined heat and power schemes of any scale. The electricity generated by such schemes is typically used in the local system rather than being transported across the UK.

### Distribution network operators (DNOs)

A DNO is a company which operates the electricity distribution network which includes all parts of the network from 132kV down to 230V in England and Wales. In Scotland 132kV is considered to be a part of transmission rather than distribution so their operation is not included in the DNOs' activities.

There are 14 DNOs in GB which are currently owned by seven different groups.

### Distribution Price Control Review 4 (DPCR4)

The price control applied to the electricity distribution network operators from 1 April 2005 until 31 March 2010.

### Distribution Price Control Review 5 (DPCR5)

The next price control to be applied to the electricity distribution network operators. This price control was implemented on 1 April 2010 and is expected to run until 31 March 2015.

### Distribution Price Control Review 6 (DPCR6)

The price control review to be applied to the electricity distribution network operators, following DPCR5. This price control would be expected to run from 1 April 2015.

### Dividend Growth Model (DGM)

The Dividend Growth Model is a method for valuing equity securities based on the present value of future dividends that are assumed to grow at a constant rate in perpetuity.

### Drinking Water Inspectorate (DWI)

The regulator responsible for monitoring and regulating the quality of drinking water in England and Wales.

## **E**

### Economic Asset Life

The period of time during which a fixed asset competitively produces a good or service of value.

### Electricity Networks Strategy Group (ENSG)

Industry focus group for network issues. The aim of the ENSG is to identify, and co-ordinate work to address the technical, commercial, regulatory and other issues that affect the transition of electricity transmission and distribution networks to a low carbon future.

### Environment Agency (EA)

The regulator responsible for monitoring and regulating environmental policy across a range of sectors in England and Wales.

### The Environmental Advisory Group (EAG)

An independent panel of environmental experts that help guide Ofgem's green agenda. The group is made up of policy experts from government, industry and the green groups who advise Ofgem on the priorities for its work in relation to the environment.

### Department of Energy and Climate Change (DECC)

### Energy and Climate Change Select Committee

Appointed by the House of Commons on 19 January 2009, this committee of 14 members examines the expenditure, administration and policies of the Department of Energy and Climate Change (DECC) and its associated public bodies.

### Energy Intensive Users Group

An umbrella organisation that represents the interest of intensive industrial energy consumers. Its objective is to achieve fair and competitive energy prices for British industry.

## The Energy Networks Association (ENA)

A trade body that represents the gas and electricity transmission and distribution companies in the UK.

## Energy service company (ESCO)

A company offering a broad range of energy solutions. ESCOs can take a variety of forms ranging from companies offering advice on energy efficient solutions to those providing a commitment to deliver the benefits of energy, such as comfort, refrigeration or industrial scale heating through linking low carbon energy sources to communities.

Established ESCOs range from Business-to-Business subsidiaries of large internationally controlled companies such as oil companies or energy utilities to small local ESCOs operating in a restricted area, often on the basis of some public-private partnership, for example that found in Woking.

## Energy service retail model

A model where energy suppliers provide customers with some form of additional services beyond supplying units of gas and electricity, for instance, offering them the opportunity to combine the cost of energy and purchase more energy efficient appliances e.g. heat pumps under contract.

## Department for Environment, Food and Rural Affairs (DEFRA)

## European Union Emissions Trading Scheme (EU ETS)

A cap and trade scheme in which EU Member State Governments are required to set emissions limits for all installations in their country covered by the scheme. It is an administrative approach used to reduce the cost of pollution control by providing economic incentives for achieving reductions in the emissions of greenhouse gases.

## Ex ante

Refers to a value or parameter established upfront (e.g. at the price control review to be used in the price control period ahead).

## Ex post

Refers to a value or parameter established after the event (e.g. following commencement of the price control period).

## F

## Fast money

Fast money allows network companies to recover a percentage of total expenditure within a one year period. For example, in DPCR5 - business support costs, non-operational Capex and 15% of all other total expenditure was received as 'fast money' with the rest being capitalised into the RAV (slow money).

## Feed in tariffs (FITs)

The price per unit of electricity that a utility or supplier has to pay for renewable electricity from private generators. These are used to encourage distributed renewable generation through private generators.



## Financeability

Financial models are used to determine whether the regulated energy network is capable of financing its necessary activities and earning a return on its regulated asset value (RAV) under the proposed price control. This financeability is assessed using a range of different financial ratios.

## Financial structure

The way in which a company finances its assets, for example through short-term borrowings, long-term debt and shareholder equity.

## Forecast business plan questionnaire (FBPQ)

The FBPQ is the forecast business plan questionnaire through which data is collected on the business plans of the 14 distribution network operators to help Ofgem form initial views on the revenue requirements of the companies for price control reviews.

## Franchising

The provision (subject to conditions) of a protected or exclusive right to exploit or carry out an activity for a given time period. Businesses will often bid for this exclusive right and in this respect, franchising is sometimes described as serving to replace competition in a market with competition for the market.

## Fuel poverty

A fuel poor household is defined as one that needs to spend 10% or more of their household income on all fuel use in order to maintain a satisfactory heating regime.

## **G**

### Gas distribution networks (GDNs)

GDNs transport gas from the National Transmission System to final consumers and to connected system exit points. There are currently eight GDNs in Great Britain which comprise twelve local distribution zones, owned by four groups.

### Gas Distribution Price Control Review (GDPCR)

The review of the price control applying to gas distribution networks. The review extended the existing price control for the year 2007-08 and reset the control for the five year period commencing 1 April 2008.

### Gas and Electricity Markets Authority (GEMA)

(See the Authority/ Ofgem)

### Gas transporter (GT)

The holder of a Gas Transporter's licence in accordance with the provisions of the Gas Act 1986.

## Gearing

Gearing is the level of indebtedness of a company. It is generally measured as net debt as a percentage of the company's total capital.

## Gilts

A bond issued by the UK government.

## Guaranteed standards of performance (GSOPs)

Guaranteed Standards set service levels to be met in each individual case and are established by a Statutory Instrument. If the licence holder fails to provide the level of service required, it must make a payment to the customer affected subject to certain exemptions.

## Guiding mind

A body which would give network companies guidance on what the relevant policy objectives are and, in some cases, what needs to be done to deliver them.

## H

### Heat and Energy Saving Strategy Consultation

A consultation document jointly published by the Department for Energy and Climate Change (DECC) and the Department for Communities and Local Government (CLG). The document sets out the Government's vision up to 2020 and beyond, and seeks views on a range of policies which could help to decarbonise the way homes and business are heated.

### The Health and Safety Executive (HSE)

A public body responsible for regulating health and safety in Great Britain with the primary function to secure the health, safety and welfare of people at work and to protect others from risks to health and safety from work activity.

### .High Level Advisory Group

A team of experts established by the RPI-X@20 project who input into our overall strategy without analysing the more intricate details.

### High voltage (HV)

Includes all voltage levels above 1kV up to and including 20kV.

### Horizontally integrated company

A company which expands its business into different products that are similar to current lines.

## I

### Incentive rate (efficiency)

The percentage of underspends/overspends against expenditure allowed at the price control review that is kept by the company responsible. The remaining savings/losses are passed through to consumers.

### Incumbent (parties)

The company that holds the position of managing and owning network assets.

### Independent distribution network operator (IDNO)

Any electricity distribution company whose licence was granted after 1 October 2001 is defined as an IDNO. IDNOs do not have distribution services areas. They own and operate electricity distribution networks which are predominantly extensions to the incumbent networks (e.g. to serve new housing developments). These companies are allowed to operate independently of the DNOs under the Utilities Act 2000.

### Independent gas transporter (IGT)

IGTs are Gas Transmission licence holders that own and operate small local gas networks.

### Inflation index

This is a measure of the changes in given price levels over time. A common example is the Retail Prices Index (RPI), which measures the aggregate change in consumer prices over time.

### Information Quality Incentive (IQI)

The IQI mechanism incentivises Distributed Network Operators and Gas Distribution Network Operators not to inflate their expenditure forecasts. It does this in two ways: by giving additional income to companies who forecast spend close to our assessment; and by providing these companies with a higher incentive rate than those companies with higher capex forecasts, thereby increasing their rewards for outperformance.

### Innovation Funding Initiative (IFI)

The IFI is intended to encourage network companies to invest in appropriate research and development activities that are designed to enhance technical development of the networks and to deliver value (i.e. financial, supply quality, environmental, safety) to end consumers.

### Interconnector

Equipment used to link electricity systems, in particular between two Member States.

### Intermittent generation

Electricity generation technology that produces electricity at irregular and, to an extent, unpredictable intervals, e.g. wind turbines.

## **J**

### Judicial review mechanism

A type of court proceeding which allows parties to challenge Ofgem's price control decision due to a perception that a flawed process had been followed or that the proposals were irrational.

## L

### Large Combustion Plant Directive (LCPD)

The LCPD aims to reduce acidification, ground level ozone particles throughout Europe by controlling emissions of sulphur dioxide (SO<sub>2</sub>), nitrogen oxide (NO<sub>x</sub>) and dust (particulate matter (PM)) from large combustion plants (LCPs). These include plants in power stations, petroleum refineries, steelworks and other industrial processes running on solid, liquid or gaseous fuel.

### Large User Group (LUG)

A key forum for engaging with business customer representatives. The LUG is open to large sized users of energy, for example metal manufacturers such as Corus.

### Licence conditions (obligations)

An obligation placed on the network companies to meet certain standards of performance. The Authority (GEMA) has the power to take appropriate enforcement action in the case of a failure to meet these obligations.

### Light handed regulation

A type of regulatory approach that is intended to place a lower administrative burden on the regulated company and the regulator, in particular by avoiding the regulator setting detailed ex ante price controls.

### Liquefied Natural Gas (LNG)

LNG is natural gas that has been condensed into a liquid at atmospheric pressure by cooling it to approximately -163°C. LNG is transported by specifically designed vessels and stored in specially designed tanks. LNG is approximately 1/600<sup>th</sup> the volume of natural gas, making it much more cost efficient to transport over long distances where pipelines do not exist.

### Load-related expenditure (LRE)

The installation of new assets to accommodate changes in the level or pattern of electricity or gas supply and demand.

### Logging up

A type of uncertainty mechanisms, logging up is a provision that a company will be compensated for all, or part, of its actual expenditure on a particular activity or area, through the revenue allowance set at the next price control review.

### Long run average incremental costs (LRAIC)

The additional costs, over the long run, of a company providing a defined increment of output (or a defined service), assuming that it already provides other defined outputs or services. Estimates of this cost measure can be used to set price limits for regulated companies.

### Long-term Energy Network Scenarios (LENS)

A study which looks at a range of future scenarios for electricity networks that could arise as a consequence of market and policy developments.

### Low carbon economy

An economy which has a minimal output of greenhouse gas emissions.

### Low Carbon Networks (LCN) fund

A mechanism introduced under the fifth distribution price control review to encourage the DNOs to use the forthcoming price control period to prepare for the role they will have to play as GB moves to a low carbon economy. The fund will see up to £500m made available for DNOs and partners to innovate and trial new technologies, commercial arrangements and ways of operating their networks.

### Low voltage

All voltage levels up to and including 1kV.

## **M**

### Market to Asset Ratios (MAR)

The MAR represents the ratio between the market enterprise value of a regulated network and its regulatory asset value (RAV).

### Micro-generation

The small-scale generation of heat and/or electricity from a low carbon source, for example solar panels, micro-wind, micro combined heat and power, and heat pumps.

### Micro-management

Exercising detailed control over the day-to-day operations of a company. This may include the regulator exercising close control over the company's management and project decision making.

## **N**

### National Electricity Transmission System (NETS) System Operator (SO)

The entity responsible for operating the GB electricity transmission system and for entering into contracts with those who want to connect to and/or use the electricity transmission system. National Grid is the GB electricity transmission system operator.

### National Grid Electricity Transmission (NGET)

NGET owns and maintains the high-voltage electricity transmission system in England and Wales.

### National Grid Gas (NGG)

The gas transporter (GT) licence holder for the North West, West Midlands, East England and London GDNs. NGG also holds the GT licence for the gas transmission system.

### National Transmission System (NTS)

The high pressure gas transmission system covering Great Britain; owned and operated by National Grid.

### National Transmission System (NTS) System Operator (SO)

The entity responsible for operating the GB gas transmission system and for entering into contracts with those who want to connect to and/or use the gas transmission system. National grid is the GB gas transmission system operator.

### Negotiated Settlement

In some regulatory regimes (e.g. energy in Florida and parts of Canada) the regulated business can negotiate a settlement with its consumers, and other stakeholders potentially, on investment and charges. The regulator may only intervene where there is a concern with the proposed agreed settlement.

### Net Present Value (NPV)

NPV is the discounted sum of future cash flows, whether positive or negative, minus any initial investment.

### Network charges

These are charges set for the use of network services.

### Non-load related Capex

The costs of the day to day operation of the network such as staff costs, repairs and maintenance expenditures, and overheads.

### Notional company/business

A notional company in this context is a hypothetical, but typical, network company.

## O

### Offshore transmission

The majority of offshore generation will be connected to the GB electricity grid through offshore transmission cables. Offshore transmission is defined as being any offshore transmission network that operates at 132kV or above.

### Operating expenditure (Opex)

Expenditure on operating and maintaining the network, e.g. fault repair, tree cutting, inspection and maintenance, engineering and business support costs.

### Option value

The potential value of a resource for future (direct or indirect) use.

## Outcomes (objectives of new regulatory framework)

What the network companies are expected to deliver. The outcomes that we expect from the new framework are that network companies play a full role in the delivery of a sustainable energy sector and deliver value for money network services for existing and future consumers.

## Outputs

Output information is to be used to assess network company performance against the outcomes within a control period. This information may be both qualitative and quantitative in nature.

## Outsourcing

A variant of a tender process that would be run by the incumbent, who would continue to decide solutions. The incumbent may make decisions on the type of investment to be undertaken for example, but may outsource aspects of delivery to an external party.

## Overall standards of performance (OSOP)

Overall standards of performance set minimum average-levels of performance in areas where it is not necessarily appropriate to put in place guarantees for individual consumers. These are determined separately for each gas transporter by the Authority.

## P

### $P_0$

$P_0$  refers to the level of cost reductions that regulated companies are required to pass on to customers at the beginning of new price control periods. The  $P_0$  figure is intended to reflect the change in allowances under the new price control as compared with the allowances that were available under the existing control.

## Pension Protection Fund (PPF)

The Pension Protection Fund established to pay compensation to members of eligible defined benefit pension schemes, when there is a qualifying insolvency event in relation to the employer and where there are insufficient assets in the pension scheme to cover Pension Protection Fund levels of compensation.

## Per Unit Depreciation

Per Unit Depreciation is a method of depreciation which tries to accurately reflect the actual use of the asset. An asset is depreciated each year by dividing the total use of the asset within that year by the expected total usage of the asset and multiplying this by the Gross Book Value.

## Post-Maintenance Interest Cover Ratio (PMICR)

A key cash flow ratio calculated by Credit Rating Agencies to assess the financial health of a regulated network company. It is a variation on the more typical FFO/interest cover ratio but reduces the contribution of regulatory depreciation to allowed revenue (and thus FFO). Some Rating Agencies believe that PMICR enables a greater degree of comparability between network companies across regulatory frameworks.

### Price control (control)

The control developed by the regulator to set targets and allowed revenues for network companies. The characteristics and mechanisms of this price control are developed by the regulator in the price control review period depending on network company performance over the last control period and predicted expenditure in the next.

### Primary outputs

Under RPI-X@20 recommendations, primary outputs concern aspects of the services that network companies provide to consumers (including network users such as generators and shippers). Primary outputs also cover network companies' impact on the environment and compliance with safety obligations.

### Priority Services Register (PSR)

PSR includes domestic consumers who are of pensionable age, have a disability, have long term ill health, and/or are blind or visually impaired. Individuals on this register qualify for a selection of free services by gas and electricity suppliers.

### Procurement

The act of acquiring or obtaining something. For example, services that assist in business operations.

### Public contest method

This is a regulatory approach in which asset expansion decisions are determined by users, as opposed to the network company or the regulatory body.

### Public sector obligation (PSO)

Public sector obligations are requirements set by a government for regulated companies to take actions considered to be in the best interests of society. For instance, meeting targets aiding vulnerable energy customers or to meet environmental targets.

### Pure price cap regulation

The regulated firm is given a maximum price it is permitted to charge for a fixed period, by the regulator.

## **R**

### Rate of return regulation

Allows a regulated body to recover the costs associated with providing a set of regulated services, including an allowable rate of return on its regulated asset base.

### Reducing Balance depreciation

Reducing Balance depreciation ensures that the value of an asset is depreciated at a gradually smaller rate throughout its useful life. It is calculated by depreciating the Net Book Value of the asset (i.e. the Gross Value minus previous years' depreciation) by a fixed percentage each year.



### Real Price Effect (RPE)

Increases/decreases in prices over and above increases/decreases in the Retail Prices Index (RPI). For example, changes in the cost of copper, steel, direct or contract labour over and above changes in RPI.

### Registered Power Zones (RPZ)

RPZ is a mechanism to encourage DNOs to develop and demonstrate new and more cost effective technologies for connecting and operating generation on their distribution.

### Regulatory Asset Value (RAV)

The RAV is a regulatory construct that reflects a company's historical investment, adjusted for inflation (currently RPI). The RAV is calculated by summing an estimate of the initial market value of each company's regulated asset base at privatisation and all subsequent allowed additions to it at historical cost and deducting annual depreciation amounts. The revenues that companies are allowed to earn under their price controls include allowances for the regulatory depreciation and also for the return investors are expected to require for providing the capital.

### Regulatory burden

A term used to describe the cost – both monetary and opportunity – of regulation.

### Regulatory Instructions and Guidance (RIGs)

A document that is published as part of the price control settlement which sets out further detail on how the price control is to be implemented and how compliance with it will be monitored.

### Regulatory reporting packs (RRPs)

The price control review information submitted annually to Ofgem under standard licence condition 52 in accordance with (and in the form and content prescribed by) the price control review reporting rules.

### Renewable Heat Incentives (RHI)

The Renewable Heat Incentive (RHI) is planned for launch in April 2011 to provide financial assistance to generators of renewable heat, and producers of renewable biogas and biomethane.

### Renewables Obligation (RO) and Renewables Obligation Scotland (ROS)

The RO places an obligation on licenced electricity suppliers in the United Kingdom to source an increasing proportion of electricity from renewable sources. Suppliers meet their obligations by presenting Renewables Obligation Certificates (ROCs) or payment into the buy-out fund.

### Renewables Obligation Certificates (ROCs)

A transferable certificate received by eligible renewable generators for each MWh of electricity generated. ROCs are traded separately from power and are used by suppliers to fulfil their Renewables Obligations under the Utilities Act 2000.

## Re-openers

A mechanism used by Ofgem to alter or re-set the revenue allowances (or the parameters that give rise to revenue allowances) under a price control before the next scheduled price control review.

## Repex

Repex refers to replacement expenditure required by gas distribution companies to comply with the Health and Safety Executives (HSE's) Mains Replacement Programme.

## Research and development (R&D)

Creative work undertaken in order to increase knowledge, and used to create new processes or technologies that will advance capabilities.

## Retail Prices Index (RPI)

The RPI is an aggregate measure of changes in the cost of living in the UK. It differs from the CPI in that measures changes in housing costs and mortgage interest repayments, whereas the CPI does not, they are calculated using different formulae and have a number of other more subtle differences.

## Return on Regulatory Equity (RoRE)

The financial return achieved by shareholders in a licensee during a price control period from its out-turn performance under the price control. The return is measured using income and cost definitions contained in the price control regime (as opposed to accounting conventions) and is expressed as a percentage of (share) equity in the business. Importantly, in the calculation the gearing (proportions of share equity and debt financing in the RAV) and cost of debt figures used are those given as the 'assumed' levels in the relevant price control final proposals. The aim of the RORE measure is to provide an indication of the return achieved by the owners of a licensee which can be compared to the cost of equity originally allowed in the price control settlement and to the return achieved by other licensees on an equivalent basis.

## Revenue driver

A means of linking revenue allowances under a price control to specific measurable events which are considered to influence costs. An example might be to allow a specified additional revenue allowance for each MW of new generation connecting to the network. Revenue drivers are used by Ofgem to increase the accuracy of the revenue allowances.

## Rolling incentive mechanisms

A mechanism which allows the company to retain a percentage of any underspends/overspends for a fixed period (usually five years) regardless of when the saving was made.

## RPI-X

The form of price control currently applied to energy network monopolies. Each company is given a revenue allowance in the first year of the control period. The price control then specifies that in each subsequent year the allowance will move by 'X' per cent in real terms.

## S

### Secondary Deliverables

Indicators of performance which may be used in support of the companies' required primary outputs

### Second Strategic Energy Review

On November 2008, the EU proposed a wide ranging energy programme. In particular it is intended to: build up solidarity between member states on energy issues; stimulate energy network investment to facilitate low carbon energy sources; secure sustainable energy supplies through a 'Security and Solidarity Action Plan'; and promote greater efficiency in use of energy.

### Scottish Hydro-Electric Transmission Limited (SHETL)

The electricity transmission licensee in northern Scotland.

### Scottish Power Transmission Limited (SPTL)

The electricity transmission licensee in southern Scotland.

### Service level agreements

Commitments from the network companies to their customers regarding the quality of service that they will provide.

### Shrinkage

Shrinkage is a term used to describe gas either consumed within or lost from a transporter's system. For example shrinkage can result from gas transmission companies using gas within their transportation systems to fuel gas compressors. Gas leaks from distribution mains are vented by certain types of equipment and shrinkage also occurs when gas is stolen or not charged for in error.

### Sliding-scale regulation

A compromise between rate of return regulation and price cap regulation. This term is used generically to describe incentive schemes which involve profit (and loss) sharing around a fixed target of costs.

### Slow money

Slow money is where costs are added to the RAV and therefore, revenues are recovered slowly (e.g. over 20 years) from both current and future consumers.

### Small and Medium User Group (SMUG)

A key forum for engaging with business customer representatives. The SMUG is open to small and medium sized users of energy, for example consumer groups such as the Federation of Small Businesses or the British Chambers of Commerce.

## Smart grid

A Smart grid is an electricity network that can intelligently integrate the actions of all the users connected to it - generators, consumers and those that do both - in order to efficiently deliver sustainable, economic and secure electricity supplies.

## Smart metering

Advanced gas and electricity metering technology that offers customers more information about, and control over, their energy use (such as providing information on total energy consumption in terms of value, not only volume), and/or allows automated and remote measurement.

## Speed of money

The speed of money in this context is the rate at which the network companies receive a certain percentage of their total expected costs. The speed of money is therefore a way of apportioning costs between both current and future consumers. (See Fast money and slow money)

## Stakeholder

Stakeholders are those parties that are affected by, or represent those affected by, decisions made by network companies and Ofgem. As well as consumers, this would for example include Government and environmental groups.

## Straight line depreciation

Straight Line depreciation depreciates the asset value in a linear fashion throughout its useful life. It is calculated by dividing the Gross Book Value of an asset by its expected useful life.

## Sulphur Hexafluoride (SF<sub>6</sub>)

A potent greenhouse gas frequently used in electrical equipment.

## Sum-Of-Years' Digits

Like Reducing Balance depreciation, Sum-Of-Years' Digits depreciation results in a more accelerated depreciation than Straight line. It is calculated by first adding each year's digits, over the depreciation period. So for instance, with a depreciation of 5 years, this would be  $1+2+3+4+5=15$ . Next, the depreciation for each year is calculated by dividing the asset's number of useful years left (in year 2 for instance, this would be 4), by the sum-of years' digits (15). This figure is then multiplied by the Gross Book Value of the asset to give the depreciation for that year.

## Supplier hub

The supplier hub principle states that the customer's principle relationship should be with their supplier.

## Supply chain

Refers to all the actors involved in the delivery of electricity and gas to the final consumers - from electricity generators and gas shippers, through to electricity and gas suppliers.

## Sustainable development

Refers to economic development which meets the needs of the present without compromising the ability of future generations to meet their own needs.

## Sustainable energy sector

A sustainable energy sector is one which promotes security of supply over time; delivers a low carbon economy and associated environmental targets; and delivers related social objectives (e.g. fuel poverty targets).

## T

### Tendering

The use of a competitive process to select a party to undertake specific projects or deliver solutions to specific outcomes.

### Third Internal Energy Market Legislative Package (The Third Package)

The third package is a key step in implementation of internal EU energy market. It recognises the need for better co-ordination between European network operators and continuing co-ordination between regulators at that level. It continues many of the internal market principles identified above in relation to the earlier First and Second Packages.

### Threshold regulation

A price threshold is set by the regulator; any firms found to be breaching this threshold may be investigated and subjected to a price control.

### Total factor productivity (TFP)-based regulation

Under TFP-based approaches to regulation, the regulator's focus when reviewing the price (or revenue) limit is on adjustments to the current limit through analysis of productivity growth (e.g. trends in measures of total factor productivity (TFP) within an industry) and, potentially, input price trends.

### Traffic Management Act (TMA)

The Traffic Management Act is intended to provide better conditions for all road users through proactive management of the national and local road network.

### Transmission Access Review (TAR)

Following the publication of the Energy White Paper 2007, the government and Ofgem convened a joint review of the current framework for access to the GB transmission system. The review explored a range of issues associated with the technical, commercial and regulatory arrangements, with the chief aim being to better support the delivery of the government's aspiration of 20 percent of electricity supplied by renewable generation by 2020 and any targets that may be agreed at European Union level.

### Transmission Owner (TO)

There are three separate high-voltage transmission Owners in Great Britain: National Grid Electricity Transmission plc (NGET) - owns and maintains the high voltage electricity transmission system in England and Wales. They also have

the role of system operator (SO) across the whole of Great Britain. Scottish Hydro-Electric Transmission Limited (SHETL) - the electricity transmission licensee in northern Scotland. Scottish Power Transmission Limited (SPTL) - the electricity transmission licensee in southern Scotland.

National Grid Gas NTS is the gas Transmission Owner.

#### [Transmission Price Control Review 4 \(TPCR4\)](#)

TPCR4 established the price controls for the transmission licensees which took effect in April 2007 for a 5-year period. The review applies to the three electricity transmission licensees, National Grid Electricity Transmission, Scottish Power Transmission Limited, Scottish Hydro-Electric Transmission Limited and to the licensed gas transporter responsible for the gas transmission system, NGG.

#### [Transmission System](#)

The system of high voltage electric lines providing for the bulk transfer of electricity across GB.

#### [Transmission system operator \(TSO\)](#)

See System Operator

## **U**

#### [Uncertainty mechanisms](#)

Uncertainty mechanisms allow changes to the base revenue during the price control period to reflect significant cost changes that are expected to be outside the company's control. Examples include revenue triggers and volume drivers.

#### [The UK Low Carbon Transition Plan](#)

A government plan plotting how the UK will meet the 34 percent cut in emissions on 1990 levels by 2020.

#### [The UK Renewable Energy Strategy](#)

This strategy explains how and why the government intends to increase the UK's use of renewable electricity, heat and transport.

#### [Uniform Network Code \(UNC\)](#)

As of 1 May 2005, the UNC replaced National Grid Gas's Network Code as the contractual framework for the NTS, GDNs and system users.

#### [Users of the Network](#)

Companies along the gas and electricity supply chain (i.e. producers/generators, transmission and distribution networks, and energy suppliers).

## **V**

### Vanilla weighted average cost of capital (vanilla WACC)

The weighted average cost of capital using a pre-tax cost of debt and a post-tax cost of equity.

### Vertically integrated company

A company that is active at more than one level of an industry's supply chain (e.g. a company that generates electricity and also operates electricity distribution networks).

### Visionary phase

The 'visionary' phase was the first stage of the RPI-X@20 project. In this phase, we aimed to understand all of the issues affecting energy networks and network regulation, and to identify areas where change may be needed.

## **W**

### Weighted Average Cost of Capital (WACC)

This is a weighted average of the expected equity and debt for the network companies.

## **Y**

### Yardstick mechanism

Yardstick is a method of regulation where the regulator uses observations of different firms' costs to determine the regulatory settlement.