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6th September 2010

Dear Hannah

Consultation on RPI-X@20 Recommendations

The Renewable Energy Association submits its comments on this landmark consultation that proposes to make some fundamental changes to the ways that electricity and gas transmission and distribution networks are regulated in the future. As you are aware our members work on all types of renewable power and heat projects and as well as our interest in electricity networks some of them are also concerned with issues associated with biogas injection into the gas network.

We have reviewed both the main "Recommendations" consultation and the more detailed "Implementing Sustainable Network Regulation" documents. Our overall comment is that what is recommended is an overall approach that aims to incentivise several desirable behaviour patterns from network owners and operators, but allows considerable flexibility in the precise form of price control arrangements for individual cases. How well the process delivers the intended results will therefore depend on how the tool kit of regulatory options is applied in each regulatory review.

We would like to record however our welcoming of setting the objective of regulation of network companies as encouraging them to "play a full role in delivery of a sustainable energy sector" alongside and at an equal level of importance as "to deliver long-term value for money network services for existing and future consumers".

We now address some of the specific matters that you have requested comments on.

Chapter 2 Introducing Sustainable Network Regulation

The recommendations are:

1 Objective: The overriding objective of energy network regulation is to encourage energy network companies to:

- » play a full role in the delivery of a sustainable energy sector; and
- » deliver long-term value for money network services for existing and future consumers.

and

2 Industry structure: The framework would be implemented under the current industry structure. GEMA would keep under review the need to revisit the alignment of transmission and system operator incentives in gas and electricity, any formal electricity distribution system operator role, and other issues.

As we have said we support the recommendation 1 and are particularly pleased that the delivery of a sustainable energy sector gets top billing as an objective. There is little choice other than to assume the current industry structure – clearly there may be changes, but these would be introduced as a stand-alone exercise and the regulatory regime would then have to adapt to any new structure.

Chapter 3 The Price Control Review Process

The recommendations are:

3 Enhanced engagement: Stakeholders are given greater opportunity to influence Ofgem and network company decision making through enhanced engagement.

4 Third party modification requests: We set out public guidelines on how GEMA would respond to a request from a third party that it exercise its discretionary power and refer a modification to the Competition Commission on the basis that our price control determination may operate against the public interest. We would keep under review the guidance, including considering the merits of asking government to introduce a formal right of appeal through primary legislation.

Whilst we applaud the ideal of encouraging third party involvement in the price control process it must be recognised that all third parties (like the network companies themselves) are inevitably going to argue in favour of their own interests, and therefore the role of Ofgem to balance the interests of competing stakeholders and regulate in line with its statutory duties must be maintained. In order for third party modification requests to achieve their maximum potential it is important that third parties have access to as much information as possible. We would therefore urge that no information used for price control purposes is kept confidential between the regulated entity and Ofgem unless absolutely necessary.

Chapter 4 Determining what network companies need to deliver

This chapter has one recommendation:

5 Outputs-led: The price control sets outputs that network companies are expected to deliver to ensure safe and reliable services, non-discriminatory and timely connection and access terms, customer satisfaction, limited impact on the environment and delivery of social obligations.

We support this and would for example be particularly interested in, for example, investigating the possibility of a fast track scheme for connecting generation of a size that is eligible for the feed in tariff.

Chapter 5 Encouraging longer term thinking with the price control

This chapter recommends:

6 Retaining an ex ante control: We would continue to set an upfront price control, incorporating a return on the regulatory asset value and inflation indexation. We think that it is appropriate to retain the retail prices index as the inflation index but will test our thinking over the summer before finalising our view.

7 Length of the price control: The price control would be set for eight years, with provision for a mid-period review of the outputs that network companies are required to deliver. Uncertainty mechanisms would be implemented consistent with transparent RPI-X@20 principles on the use of such mechanisms. There would be scope to review the length of the control period at future price control reviews.

We agree with the principle that to the greatest extent possible the allowed income should be set up front. In terms of the length of the price control period we think that eight years with a review of certain well defined aspects mid-term is probably a reasonable balance between allowing real incentives for long term performance improvement and not enabling large deviations from a reasonable level of return for reasons totally outside the control of the network business. It is therefore important that reasons to adjust the control midterm are confined to those resulting from changes outside the control of the regulated company.

Chapter 6 Determining the revenue to be raised from consumers

The recommendations are:

8 Proportionate assessment: We would adopt a transparent and proportionate approach to assessing the price control package, with the intensity and timescale of assessment reflecting the quality of an individual company's business plan and its record for efficient output delivery. Under this approach, we may conclude the process early for some companies.

9 Option to give third parties a greater role in delivery: We would include in the regulatory tool-kit the option to require a company to provide market testing evidence that its proposals reflect long-term value for money. We would have the option to involve third parties in delivery and ownership of large and separable projects, where this is expected to drive innovation, long-term value for money and/or more timely delivery.

10 Incentives: There would be transparent rewards/penalties related to output delivery, including a backstop threat of using our existing powers for enforcement action and potential licence revocation for persistent non-delivery. There would be transparent, upfront, symmetric efficiency incentive rates for under and overspend. Incentives would be calibrated to ensure they provide long-term value for money.

We agree that where a company has been demonstrated to give consistently good value for money (not just because of the nature of the area it operates in but because it is maximising the scope for efficient delivery within its environment) it may be given a fast track regulatory settlement. We would however, with an eight year price control period, caution against a company being allowed a fast track approach two periods running.

As regards market testing there needs to be a clear distinction between putting work out to competitive tender in the normal way and effectively taking away part of the licensed functions of a network business and giving it to another party. If this is meant as a partial license revocation then it may make some sense. Clarity is required as to whether this is the purpose – if not we are not sure what would be achieved that an ordinary subcontracting process would not.

Chapter 7 Ensuring efficient delivery is financeable

We have no comments on this chapter.

Chapter 8 Innovation stimulus package

This chapter recommends:

12 Innovation stimulus package: We would introduce a time-limited innovation stimulus for electricity and gas networks. These would be open to projects at any point in the innovation cycle and to both network companies and third parties for innovation related to delivering the networks required for a low carbon energy sector. The innovation stimulus package would include substantial prize funds to reward network companies and third parties that successfully implement

new commercial and charging arrangements to help deliver a sustainable energy sector.

We support this but would be inclined only to use the proposed facility to make an award directly to a non network company as a last resort. Third parties should generally be encouraged to submit projects in conjunction with a network company. It is only when partnership in a proposal for funding has been declined by relevant network companies and there is judged to be considerable merit in the project that direct funding of third party innovation providers should be considered.

Please let me know if you would like to discuss any of these comments further.

Yours sincerely

Gaynor Hartnell

Chief Executive, REA.