

The background features a large, semi-transparent white 'X' shape. Behind the 'X', there are two distinct images: on the left, a perspective view of solar panels under a bright sky; on the right, a close-up of interlocking mechanical gears, one of which is highlighted in a warm, golden light.

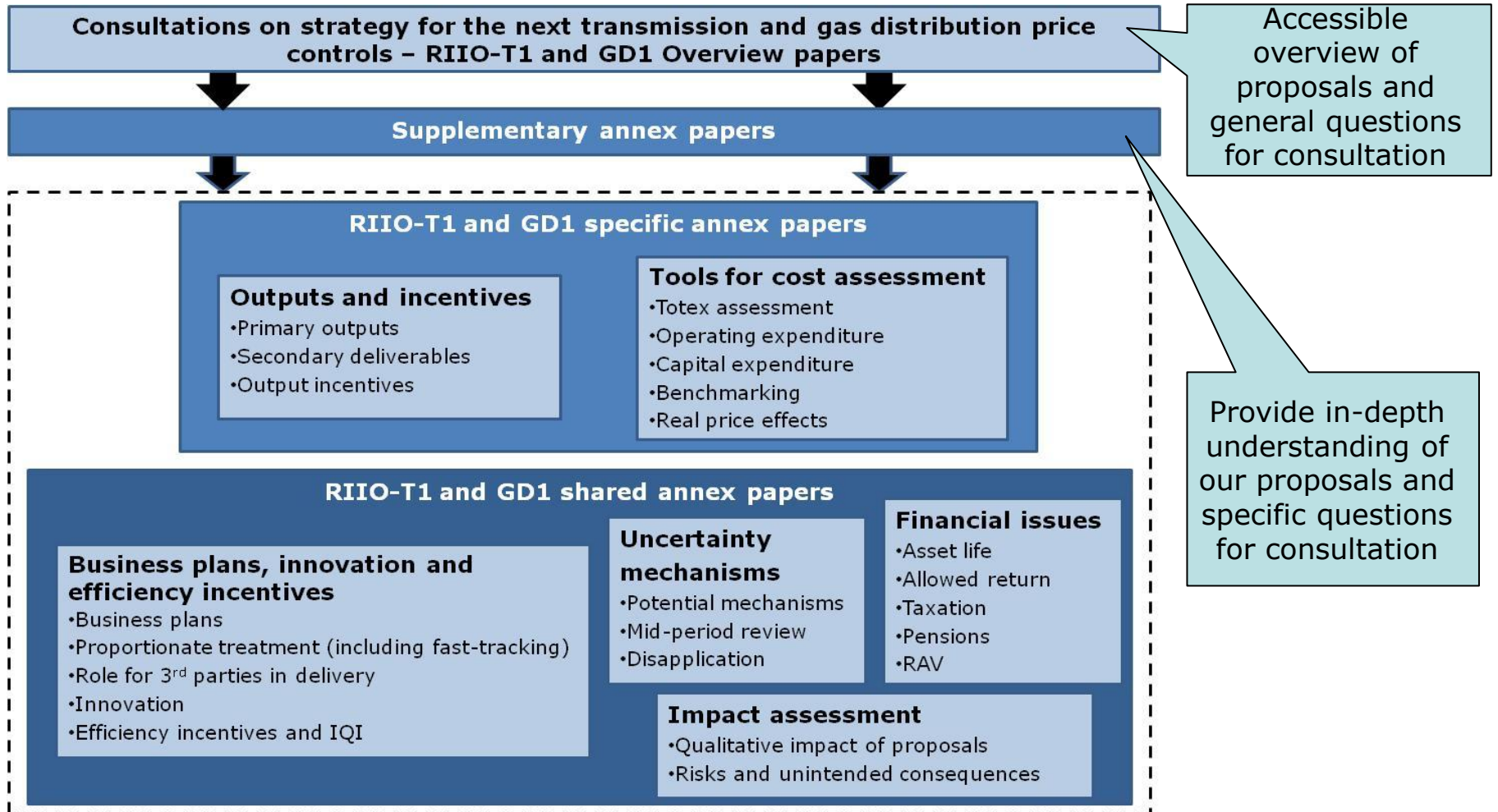
# **RIIO-T1 and GD1 Price Control Review Forum**

24<sup>th</sup> January 2011

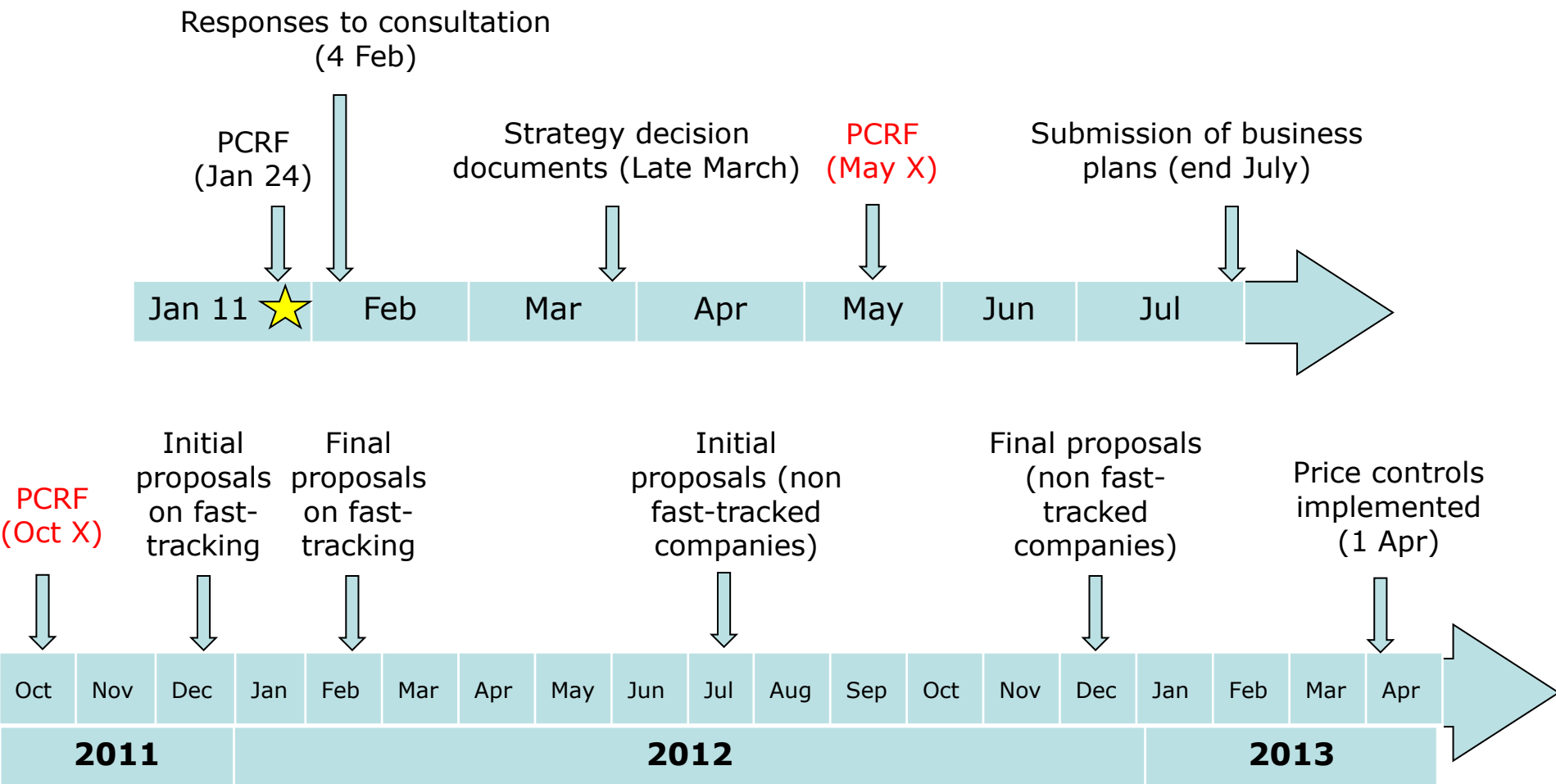
# **Session 1 – Introduction**

# Structure of the meeting

Based on December consultation documents and key issues raised.



# RIIO-T1 and GD1 timeline of forthcoming publications



## Way forward

**We appreciate contributions that stakeholders have made to RIIO-T1 and GD1 to date**

We would welcome comments on the initial strategy consultation by 4 February 2011

**We are carrying out a number of stakeholder events in early 2011**

**The PCRf and meetings of  
the Consumer Challenge  
Group**

**Further output working group  
meetings to develop thinking on  
the measures and incentives**

**City event (1  
Feb )**

**Financial issues working group  
(12 Jan & 17 Feb)**

**An opportunity for TOs and GDNs to meet  
with our Committee of the Authority**

**TOs and GDNs should also continue their stakeholder engagement during this period**

**We intend to publish a strategy decision document at the end of March 2011**

The companies will be required to submit their business plans by end July 2011

# **Session 2 – Summary of stakeholder engagement**

## Network companies' stakeholder engagement

Update from network companies on their engagement to date and future plans (max 5 mins):

- What have you learnt from your engagement to date?
- How do you intend to use this information to inform your business plan?
- What are your engagement plans?

Questions for network companies on their engagement from PCRf members

# **Session 3 – Views of Generators and Shippers on the proposed RIIO-T1 and GD1 outputs and incentives**

**Presentation by EDF Energy**



# **Session 4 – Overview of December documents**

# Incentivising output delivery

## Developing the outputs-led framework

**Primary outputs** = reflect services network customers receive during the price control.

**Secondary deliverables** = outputs that network companies will be held to deliver in the coming price control to ensure the delivery of primary outputs in future periods

Consistent with RIIO handbook principles

**We expect network companies to propose the output levels they intend to deliver**

Network companies should justify these levels based on costs and benefits to consumers

### Range of output incentives

Financial rewards/  
penalties



Symmetric, or  
penalty/reward only

Reputational  
incentives

Secondary deliverables  
monitored annually

**Incentive  
strength**

Strength of incentives will reflect value consumers attach to delivery and degree of network's control

**Risk sharing**

Mechanisms will ensure efficient risk sharing between companies and consumers

**Delivery of primary outputs will be monitored using a balanced scorecard**

## RIIO-T1: Potential outputs and incentives

Output category	Output name	Incentive
Safety	Compliance with legal requirements set by HSE and other bodies	No financial incentives
	Suite of secondary deliverables to monitor asset risk	Potential financial incentives if material over/under delivery of asset risk
Reliability & availability	Minimise energy not supplied (elec)	Financial incentive approx £16k per MWH - Natural cap on reward; Uncollared penalty
	Reliable delivery of gas to users (gas)	Financial incentives based on existing framework
	Potential secondary deliverable for network system flexibility (gas)	Potential financial incentive
	Suite of secondary deliverables to monitor asset risk	Potential financial incentives if material over/under delivery of asset risk
Customer satisfaction	Customer satisfaction survey	Symmetric financial incentive +/- 0.5% of revenue
	Effective stakeholder engagement	Discretionary reward +0.5% of revenues

## RIIO-T1: Potential outputs and incentives

Output category	Output name	Incentive
Environmental impacts	<p>'Low carbon economy' – networks' contribution to UK's environmental goals e.g.</p> <ul style="list-style-type: none"> <li>Emission intensity of network energy flows</li> <li>% renewable of network energy flows</li> </ul>	Potential financial reward or reputational incentive
	Losses (elec)/shrinkage (gas)	Potential symmetric financial incentive
	Business carbon footprint	No financial incentive – reputational
	Release of SF <sub>6</sub> (elec)	Symmetric financial incentives building on current framework and rollover proposal
	Release of Methane (gas)	Potential symmetric financial incentive
Connections	<ul style="list-style-type: none"> <li>Timing of preconnection period (elec)</li> <li>Timing of build (gas)</li> </ul>	Further data sought to understand the degree of financial incentives (if any)
Social	No outputs proposed	NA

## RIIO-GD1: Potential outputs and incentives

Output category	Output name	Incentive
Safety	Compliance with HSE safety case (in particular emergency response and repair activities) and level of risk removed associated with repex	Requirement to comply with safety case and licence. For repex propose to use a revenue driver based on risk removed rather than length abandoned.
Reliability & availability	Number and duration of interruptions to supply	Incentivised as part of Guaranteed Standards. Secondary output covered by asset health measures.
	Maintaining operational performance (incl. offtake meter error management)	Reputational
	Suite of secondary deliverables to monitor asset health	Potential financial incentives if material over/under delivery asset health ( <b>covers multiple output categories</b> )
	Network capacity: Meeting 1 in 20 obligations	Ex-post review of asset utilisation against target
Customer satisfaction	Customer satisfaction survey	Symmetric financial incentive +/- 0.5% of revenue
	Effective stakeholder engagement	Discretionary reward +0.5% of revenues
	Complaints handling	Penalty -0.5% of revenue

## RIIO-GD1: Potential outputs and incentives

Output category	Output name	Incentive
Environmental impacts	Reducing gas shrinkage and associated carbon emissions	Symmetric financial incentives on shrinkage and associated carbon emissions building on existing incentives
	Business carbon footprint	No financial incentive – reputational
	% biomethane connected to the network	No financial incentive – reputational
	Networks' non-CO <sub>2</sub> emissions and resource use (inc. gravel extraction and water emissions)	No financial incentive – reputational
Connections	Timely connection for users of the network (inc. Gas entry customers)	Extension of existing financial penalties potentially akin to DPCR5
Social	Carbon monoxide risk awareness	No specific incentives
	Information on network extensions for fuel poor	No specific incentives. Review of existing funding arrangements

## Repex – gas distribution

### **HSE led review of repex**

- CEPA appointed
- Draft findings by end of February
- Final report by end of March
- HSE will then consider the results of this work

### **Change to repex driver**

- Move to a risk removed driver

### **Development of asset health and risk metrics for all assets**

- Requiring GDNs to improve their current understanding of asset health and criticality, and to develop systems to optimise and plan investment on the basis of risk indices.



## Questions for forum members

- Do you consider the proposed outputs and associated incentives, along with the other elements of the proposals, will ensure companies deliver value-for-money for consumers and play their role in delivering a sustainable energy sector?
- Do you consider that the proposed outputs and incentive arrangements are proportionate?
- Do you have any views on the proposed outputs?
- Do you have any views on the proposed incentive mechanisms?
- Do you agree with the approach to changing the repex revenue driver from length of mains decommissioned to a volume driver of risk removed?

# **Business plans and proportionate treatment**

## Well-justified business plans

**Companies will be required to develop well-justified business plans setting out**

**How they will deliver in the interests of current and future consumers**

**How they will meet the challenge of moving to a low carbon economy**

**A strategy for dealing with risks and uncertainties**

**Key messages emphasised in our business plan guidance**

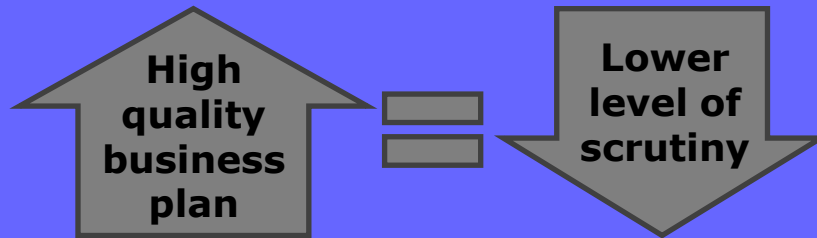
**Companies need to justify their strategy for output delivery against an understanding of the long-term trends they face**

**Companies need to show they have considered a range of stakeholder views and opportunities for innovative approaches**

**The plan should include a holistic view of the price control package including financeability metrics**

# Proportionate treatment

Under a proportionate approach the intensity and timing of assessment will reflect the quality of business plans and company records for output delivery



We have proposed 15 assessment criteria to assess quality of business plans.

High quality business plan may be **fast-tracked** - concluding its price control early.

## Key features of fast-tracking

Price control will be finalised approx 12 months before non-fast tracked companies

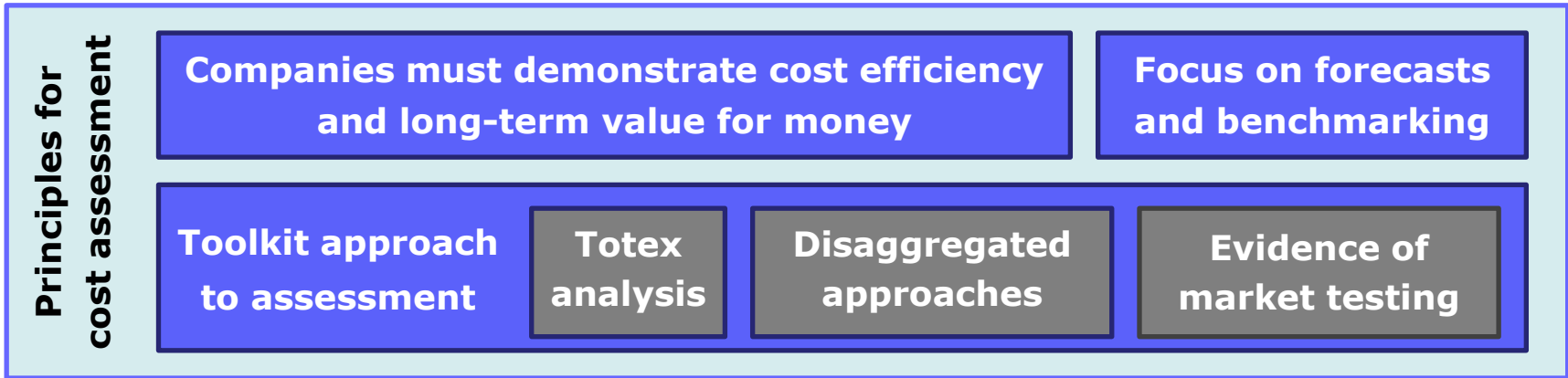
We will consult on any proposals for fast tracking

Fast-tracked companies will not be worse off than others



We do not think specific protection is needed but are seeking stakeholder views on this

## Cost assessment



**Propose the use of a fixed and symmetric efficiency rate**  
Investors /consumers will share benefits of underspend and the costs of overspend

## Criteria for assessing business plans

1. Key content
2. Acceptance of our policies
3. Structure and proportionality

**Approach the company has taken  
to the business planning process**

4. Efficiency of costs
5. Long-term context
6. Reflect uncertainty
7. Deliverability
8. Effective engagement and understanding of stakeholder views
9. Risk
10. Reflecting best practice

**The strategy underlying  
the business plan**

11. Accurate and full completion of a business plan template in a timely manner
12. Quality of information on primary outputs
13. Quality of information on secondary outputs
14. Evidence
15. Linking forecasts to historical performance

**Reflection of strategy  
in the plan**

## Questions for forum members

- Is our proposed approach to cost assessment appropriate?
- Do you have any views on our proposed process for proportionate treatment?
- Do you have any views on the criteria for assessing business plans?<sup>1</sup> Are any of the criteria highlighted inappropriate? Should any additional criteria be added?
- Do you have any views on the proposed role for competition in third party delivery?

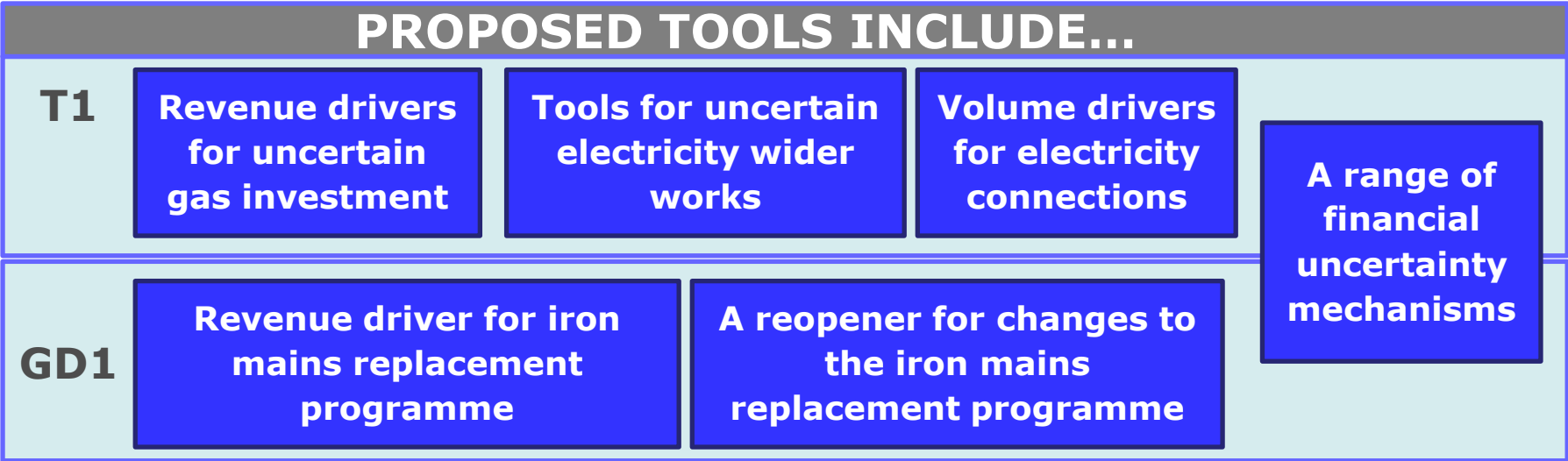
<sup>1</sup>For details of criteria see paras 3.46 – 3.74 (p.22-27) of 'Supplementary Annex - Business plans, innovation and efficiency incentives.'

# **Uncertainty mechanisms and the mid-period review**



# Managing uncertainty

**Uncertainty mechanisms allow changes to the revenues a company is allowed to collect during a price control in light of developments during the control**



## Mid-period review

Recognising the scope for significant changes in outputs over an eight year price control, RIIO includes a mid-period review of outputs



As part of the mid-period review, we will consider the risks and downsides associated with any potential changes e.g. instability of outputs



## Questions for forum members

- Do you have any views on the uncertainty mechanisms identified?
- Are there any additional uncertainty mechanisms required that we have not identified?
- Are there any mechanisms that we have included that are not necessary and, if so, why?
- Do you have any views on the scope of the mid-period review and the process?

# Innovation

# Innovation

**RIIO has a number of elements that are designed to drive innovation**

<b>Longer price control period</b>	<b>Outputs focus</b>	<b>Strong efficiency incentives</b>	<b>Companies can propose innovation in business plans</b>
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**RIIO also include an innovation stimulus for gas and one for electricity**

	<b>Innovation stimulus gas</b>	<b>Innovation stimulus electricity</b>	
<b>April 2013</b>	<b>Transmission and Distribution</b>	<b>Transmission</b>	<b>Low carbon networks (LCN) fund: Distribution*</b>

**Funding for all types of innovation e.g. R&D, trials**

**Funding available to third parties to allow them to lead innovative network projects**

**\*Expect electricity distribution to be included in the innovation stimulus in 2015**

**In addition to innovation stimulus, we propose an innovation allowance within revenue allowances: up to 2% of revenue depending on quality of innovation strategy**

# The innovation stimulus

**The innovation stimulus is being developed in parallel to the price controls**  
Three key elements will inform network companies in developing their business plans

**Amount of funding**  
Greater scope for innovation

- in distribution than transmission
- in electricity than gas

<b>Proposal</b>	<ul style="list-style-type: none"> <li>➤ Funding of £25-£35m a year in electricity transmission</li> <li>➤ Funding of £45-£50m a year for gas</li> </ul>
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**Scope of funding**

<b>Proposed approach</b>	<ul style="list-style-type: none"> <li>➤ Focused on projects to inform a low carbon future</li> <li>➤ In gas, should projects need to contribute to long-term network sustainability?</li> </ul>
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**Partial project funding**

<b>Proposed approach</b>	<ul style="list-style-type: none"> <li>➤ Propose to provide a maximum level of project funding of 80%</li> <li>➤ Decreased from 90% under LCN Fund</li> </ul>
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**This the subject of a separate impact assessment published alongside the RIIO-T1 and GD1 documents**

## Questions for forum members

- Do you have any views on the role of innovation in RIIIO-T1 and GD1?
- Do you have any views on the time limited innovation stimulus?
- Do you have any views on the inclusion of an innovation allowance within the price controls

# Financing efficient delivery



## Financing efficient delivery: Capitalisation policy and asset lives

### Capitalisation policy

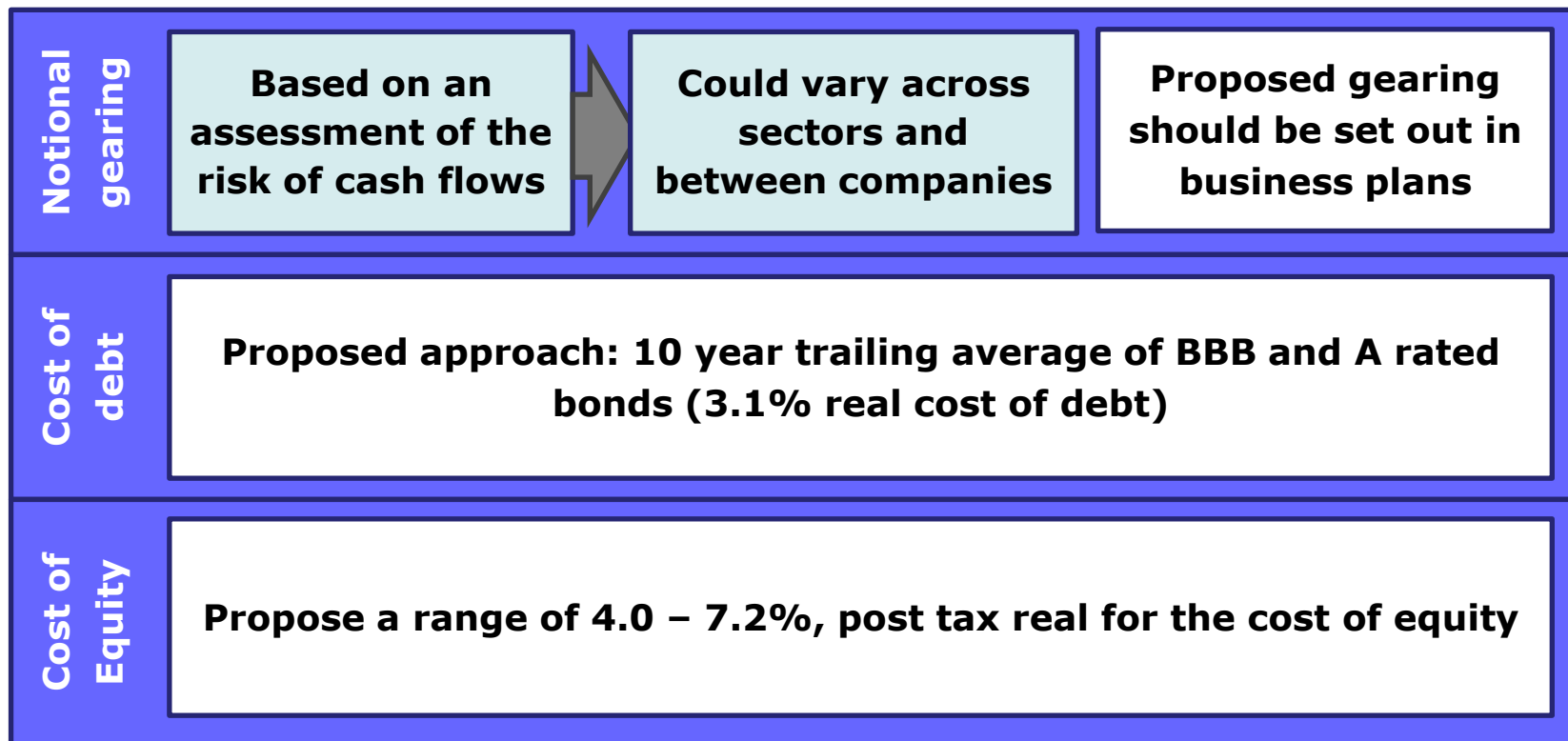
Propose that repex should be treated as investment in longer life assets with 100% capitalised

### Asset lives

- Propose to retain 45 year asset life for gas and a range of 45-55 for electricity
- Propose front end loaded depreciation profile to protect against a potential future decline in gas distribution use

May need transition arrangements for repex treatment as well as asset life changes

## Financing efficient delivery: The allowed return



## **Question for forum members**

- Do you consider that the package of financial measures identified will enable required network expenditure to be effectively financed?

# **Session 5 – Willingness to pay research on designated landscapes and RIIO-T1**

**Presentation by Campaign for National Parks**

# Session 6 – Wrap up