

Annex 3:

Response Template

Thank you for taking the time to respond to our questions.

We hope all the questions are clear, but if you have any difficulties please email rupika.madhura@ofgem.gov.uk.

Once you have completed the questionnaire please send it back to us to the email address above. You need to return the completed response template to us by **31 October 2014**.

Part 1 - About you

Question	Your response
<i>What is your name?</i>	
<i>What is your position?</i>	
<i>What are your contact details?</i>	

Part 2 - About your business

Question	Your response
<i>What is your company's name?</i>	National Grid Gas Distribution
<i>What is the nature of your company's business? Please state if this involves Fuel Poor Network Extensions Scheme, or Fuel Poverty related work.</i>	Gas Distribution – target to connect 34,650 fuel poor gas connections, including both one off and community connections, by the end of March 2021.
<i>What areas of the country does your business operate in?</i>	National Grid owns and operates four distribution networks in the England, in the North West, West Midlands, East Midlands and East Anglia, and North London.

Part 3 – FPNES review questions

Q1 Do you think the Scheme effectively interacts with the UK heating Strategic Framework and Scotland's Heat Generation Policy Statement? How might it be improved to better align with wider activity? Please evidence your answer.

With an existing gas network in place, we would support future policy that maximises the value of these assets, and reduces the risk of stranding. The use of more efficient forms of gas heating, the use of new forms of renewable gas and district heating schemes can all use the existing infrastructure, and be consistent with the strategic framework.

However, at the extremes of population density, the strategic framework suggests it is less likely that a gas solution is preferred. For rural fuel poor communities, to be consistent with

the framework, only one-off fuel poor connections to the existing gas grid would seem compatible. This is achieved with the current scheme as most rural mains extension projects are likely to be too expensive to be viable, and therefore there are limitations to how far the framework goes in meeting aim of reducing fuel poverty.

In the highest density areas, low carbon heat networks are preferred. These could be gas heated initially, with conversation in the longer term, if necessary to renewable energy without making the whole heat network redundant. The GDNs and their partners have increasing experience in delivering heat networks, and working with landlords and local authorities to deliver heating solutions. We can therefore play a key role in moving towards low carbon heating in the most heavily populated areas. The current scheme currently does not support heat networks, and National Grid has not forecast any community gas connections at all in north London in RIIO-GD1 due to the high cost and risks of bringing gas to densely populated, high rise, multiple occupancy buildings.

A household in fuel poverty should have access to the optimum solution which reduces their exposure to fuel poverty, and where possible also reduces emissions. This may not always be the provision of a new gas connection. Changes to the scheme to support alternative solutions such as off-gas grid community solutions, or alternative funding mechanisms, would therefore make the scheme more consistent with the longer term strategic framework. Whilst other non-gas organisations could also need to access funding for off-gas grid fuel poverty projects, these projects will either impact gas and electricity network, or will require the skills and capabilities developed for gas solutions by the GDNs and their partners.

Unconventional sources of gas like shale may present further opportunities to reduce fuel poverty e.g. through the extension of the gas network to rural areas currently off the gas grid, as part of the shale gas to grid connection. As with GDNs and energy suppliers, shale developers could be given obligations to support a reduction in fuel poverty in their area of operation. Alternatively, the GDNs could have a role to play in developing solutions with developers to reduce fuel poverty using shale gas.

When considering the strategic framework for heating, any decision involving renewable gas such as bio-methane should also consider the interaction with their use to reduce emissions in the transport sector, where the benefits could be greater. Another potential interaction with transport strategy is a new EU directive requiring member states to each develop a national policy roadmap to provide the infrastructure to support gas vehicles. This is being led by the Department for Transport, and the possible interaction will need to be thought through.

Q2 Should the Scheme be targeted at certain types of customers/certain locations to maximise long term benefits (e.g. over a period of 15-45 years)? If so who/which locations should be targeted and how might this best be achieved?

Currently Gas Distribution Networks (GDNs) have a target to deliver a number of fuel poor gas connections by March 2021. With a fixed allowance to deliver these targets, as with normal expenditure allowances, GDNs are incentivised to deliver these as efficiently as possible, and not to over deliver. It may also incentivise GDNs to deliver the simpler and more straightforward gas connections, rather than those that will deliver the greater benefits. These standard RIIO incentives may not be as appropriate when considering fuel poverty, where utilising the full allowance to help as many households as possible, would seem a better outcome.

An alternative approach could be to incentivise GDNs to maximise the reduction of fuel poverty or to maximise the reduction of fuel bills for households in fuel poverty. This would incentivise the GDNs to ensure their regulatory allowance delivers the most value,

and would result in the full allowance being utilised. Normally efficiencies from beating a unit cost allowance are shared with the GDN and the end consumer. Such an approach would also enable the GDNs to implement non-gas solutions.

Such a model would give the GDNs the freedom to identify which solutions and locations to prioritise, and to collaborate effectively with the other GDNs and other utility companies. Remunerating strong performance would need to be considered with such a model, as efficiency retention would not operate.

In terms of specific targeting, as discussed above, there is already some targeting due to the higher costs for network extensions to rural areas, which restricts connections to remote rural fuel poor communities, that may be better served from other measures National Grid does specifically target OGG Communities and that through its relationship with AWS we've been very good in delivering to some of the most vulnerable groups of our society.

With the uncertainty with exactly how full decarbonisation of heating would be achieved in the longer term, and the role of gas networks and renewable gas, the provision of a new gas connection to an existing main will remain the best option in many cases to reduce fuel poverty and to reduce carbon emissions in suburban areas in the short to medium term. However, this does require there to be funding available for in-house measures. Revising the scheme to recognise the probability of a full scale move away from gas for heating in the next 20 years, would seem premature, and would be inconsistent with other GDN investments which are designed and depreciated over 45 years. The time to review the targeting of this scheme over the next 15-45 years will be when there is sufficient clarity and certainty surrounding the move to low carbon heat in buildings. There will be a number of areas within which the GDNs operate that may be impacted, including this scheme.

Q3 How effectively is the Scheme interacting with these strategies and other forms of assistance? Please explain where the Scheme works well and where there are any issues.

The simplicity and transparency of the current scheme has worked well, and has been a key factor in supporting National Grid's outperformance of the initial target for fuel poor connections, and being on course to deliver our objective of at least 34,650 connections during RIIO-GD1.

National Grid has worked incredibly hard and innovatively in order to successfully reduce Fuel Poverty in what is a complex area of activity. The schemes are difficult to co-ordinate and deliver and the targeted nature of initiatives makes it a relatively high cost to resource which contributes to much higher unit costs.

National Grid's success is based upon our vision to establish a dedicated organisation to deliver our fuel poverty commitments and the efficiency of that organization to work with its customers to develop bespoke solutions to meet the needs of the community, client and customers.

Perhaps the greatest challenge we have faced is ensuring that homes receive 'in-house' measures and in particular new gas heating systems. Social Landlords are capital constrained and the closure of the Warm Front Scheme (England) has resulted in a lack of public funding for in-house measures. It should be noted that this is not the case in other GDN areas, Wales and Scotland where public funds are available to fund new heating systems. This misalignment does pose us greater challenges to other GDNs and we would welcome steps to align and coordinate funding from other schemes to fully realise the benefits of the gas connection. An example could be pointing GDN and Supplier fuel poverty funding towards each other e.g. supplier fuel poor voucher equivalent that the GDN could claim where the gas connection itself passed the economic test.

There is significant scope to incentivise non-gas solutions to reduce fuel poverty for off gas grid households and we would welcome any moves to make access to funding in these areas easier.

We have long supported the development of heat networks and have funded several pilot schemes through our partnership with AWS. Our customers tell us, that there is a demand for gas fired heat networks and we would suggest that GDN's are incentivised through the mains gas extension scheme to support such initiatives and enabling the costs of network extension (and any surplus funding from the gross value of individual FPV to be used to fund the heat network) to be recovered and recognising these connections in the network operators gas extension targets.

Q4 Are there any changes we could make to the Scheme that would better align it to these strategies and forms of assistance?

The provision of a gas connection to a community district heating scheme should be recognised as a benefit to each household affected, with cumulative funding available for each qualifying household. A mains extension to a community, which each has an individual gas connection and their own gas heating, should not be treated differently than a district/community heating scheme with a central gas boiler.

Information sharing or centralised data provision between GDNs and energy suppliers should be supported to allow the gas connection and in-house measures from the suppliers to be coordinated. This coordination could be made more efficient if the GDNs could automatically access supplier funds. For example, as discussed above, if the GDN or the homeowner/landlord could access an equivalent of a fuel poor voucher for in-house works. Then the GDN could better coordinate the installation of the gas supply and central heating systems. This greater in-house role would also facilitate raising carbon monoxide awareness in the households, and the installation of CO alarms where appropriate.

Q5 Does the Scheme provide an opportunity to address these issues What changes could be made to the Scheme to help address these issues?

The connection to off-gas grid communities is generally more expensive than a short one off service connection to an existing gas main. The funding from the fuel poor voucher is less likely to stretch to cover the full cost of this scheme. The provision of additional funds would enable the more remote fuel poor communities to be connected.

One option we would put forward for consideration would be to allow the GDN to assume all households along the route of the network extension will connect, irrespective of whether they are currently a qualifying household. This would improve the overall cost benefit analysis, and would recognise the likelihood of that property falling into fuel poverty in the future.

A second proposal for consideration would be to allow the GDNs to include an allowance for lifetime savings seen by the electricity networks. Where an off gas grid community is switching from electricity to gas for their heating requirements, a methodology could be derived to estimate the lifetime capital and operational expenditure savings the electricity network operators would see. This could be used to increase the available funding to complete the network extension.

A further idea for consideration to generate more funds to support off gas grid connections would be to explore the use of regulatory fines to provide greater scope to reduce fuel poverty. This could be refined to target such ad-hoc windfalls to the GDNs

that have shown the strongest performance in reducing fuel poverty.

Or alternatively public (treasury) funds should be in place through general taxation, a far more progressive way to fund infrastructure projects. How about if extending the gas network to rural OGG homes was made a National Infrastructure project (10 years) then this could be funded part through the regulatory and the remainder through public finance (e.g. roads / sewers etc. already use this principle)

Q6 Are there any other changes you would like to see made to the Scheme? If yes, what benefits do you think these changes will deliver?

Through National Grid's vision to develop an agile organization to collaboratively work with customers and stakeholders, we have managed to maximize our impact on reducing Fuel Poverty under the scheme. There are areas where improvements could be made.

The uncertainty created by the finite nature of our funding does present a challenge with our engagement strategy. Clearly putting up the "Closed" sign when a network reaches its target, is not the message we would want to give, but continuing to deliver fuel poor connections could present a new risk for the network. Seeking regulatory approval for funding when a target was being reached would also inevitably create a period of uncertainty which would affect investments. We would therefore welcome a more flexible funding mechanism to remove this uncertainty, and to enable longer term planning with our stakeholders.

Reaching this point could be delayed if the regulatory approach was modified to focus on maximising the benefit from spending the full allowance. For multi-network GDNs, an ability to pool allowances/targets could also extend delivery with certainty of funding. A simple revenue driver would be our preferred approach, with a sensible absolute backstop total to protect the overall level of costs being passed through to consumers. A revenue driver would need to recognise the difference in costs between a one off fuel poor connection to an existing main, compared to a community connection with a significant section of mains extension included. A revenue driver could be subject to delivering the target connections within the original regulatory allowance.

In reviewing the scheme, Ofgem may wish to verify that the scheme costs are being properly socialised. Currently, the GDNs allowed costs are recovered within the individual networks in which the costs are incurred. If there are areas of significant fuel poverty, but with relatively lower numbers of consumers, then it could be concluded that the consumers in this network are paying an unreasonably high share of the costs. This affect could be magnified with the new definition of fuel poverty, if there is a network with relatively high levels of fuel poverty, relatively high energy costs, but low numbers of consumers.

The provision of the concessionary coal allowance (administered by DECC) can be a barrier to providing more practical, energy efficient and environmentally acceptable heating systems. By providing an alternative comparable incentive for these former miners and their dependents to switch fuels could make their homes and lives more comfortable, energy efficient and at the same time make a positive impact on air quality, the environment and perhaps most importantly their health. Further benefits may be realised if an alternative funding mechanism could support whole community solutions

Q7 Do you agree with the updates to the eligibility criteria suggested in Annex 1? If not, please explain your rationale and any other changes you would like to see?

National Grid do agree with the eligibility criteria apart from the disparity between the LI/HC proxy in England and the 10% proxy in Scotland and Wales, this will probably

make is more difficult for GDN's in England to meet their targets.

Eligibility criteria will be reviewed and evolve over time, and we would look to government policy informed by strong stakeholder engagement to ensure the criteria are appropriate and fit for purpose.

From a GDN perspective, there is an interaction between our ability to hit a regulatory target for fuel poor connections, and changing criteria. However well considered, there will always be an element of uncertainty regarding how harder or easier the new criteria will make it for the GDNs to hit their targets.

As discussed above, there may be merit in considering moving away from regulation by a conventional allowance/target mechanism. Having a fixed allowance that the GDN must spend but will be measured on the benefits delivered would lessen the impact of any uncertainty as criteria evolve.

We would note that if criteria do change, the GDNs will incur costs to adapt their process and systems. For example, National Grid would have to undertake a post code mapping exercise to update the codes used to confirm eligibility for the fuel poor voucher in our on-line application system. Resource would also be taken up assessing the implication of changes and identifying and establishing any new relationships with partner organisations.

The criteria themselves should be simple, transparent, and reasonably deterministic to enable the GDNs to identify eligible consumers as efficiently and painlessly as possible. We would welcome the use of proxy measures should these simplify the process, even if they are not 100% perfect. These could evolve over time, and a mechanism for the GDNs to propose new or amended proxy measures, subject to Ofgem approval, would support delivering the maximum benefits as quickly as possible.

Q8 Do you agree with this change to the average domestic gas consumption value?

If the fuel poor voucher mechanism is used to define the level of funding available for fuel poor households to fund a gas connection, then with the current methodology, the lower the consumption value used the lower the voucher, and the lower the potential to reduce fuel poverty. To be consistent, the consumption value used should be the required gas usage for the household. However, the behaviour of a household in fuel poverty may differ from an average household e.g. tighter control of energy consumption.

The concept of the fuel poor voucher allowance provides funding aligned with the expected lifetime income stream from gas usage. This is making the gas connection self funded by the distribution income stream. This makes sense, however, there is then a disconnect between this funding available to the household, and the regulatory funding provided to the GDNs.

Our preference would be to create a holistic remuneration and funding model, where the regulatory funding for the GDNs is consistent with the funding available for fuel poor connections, and fixed for the remaining years of RIIO-GD1 (and the first years of RIIO-GD2 to avoid fuel poor work being suspended awaiting the installation of the conclusion of GD2). As National Grid has submitted costs for both one off and community connections, this approach may result in different levels of funding being made available for each type i.e. a different fuel poor voucher level for a one off connection and a community connection.

If energy consumption is used to derive a level of funding, consideration should be made

to using a different value for different types of eligible consumer. For example, if a household includes a vulnerable person, then the requirement for heating through the day may be higher and therefore the voucher level correspondingly higher.