

Towards Smart Regulation

David Gray



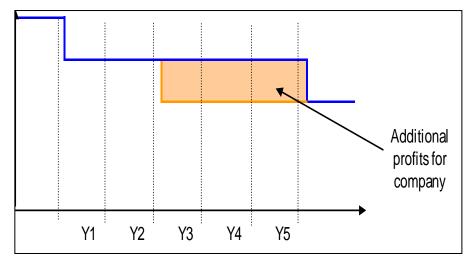


RPI-X Regulation

- Revenues set for five years
- Companies have strong incentive to cut costs
- Competitive pressure from league tables
- Substantial real decline in network charges
 - More than 30% reduction in electricity distribution charges (1990 – 2015)

Significant improvement in reliability and customer

service





RPI-X Regulation

BUT

- Companies focussed on short term
- Cyclical business flows for supply chain
- Innovation squeezed out
- Bias to capital expenditure
- Very prone to gaming





Shortcomings of RPI-X mattered more as circumstances became more complex

Ageing Assets

Many assets coming to end of useful life

Affordability

Network costs around a fifth of the typical energy bill

Network companies

Faced a number of
challenges at same time

De-carbonisation

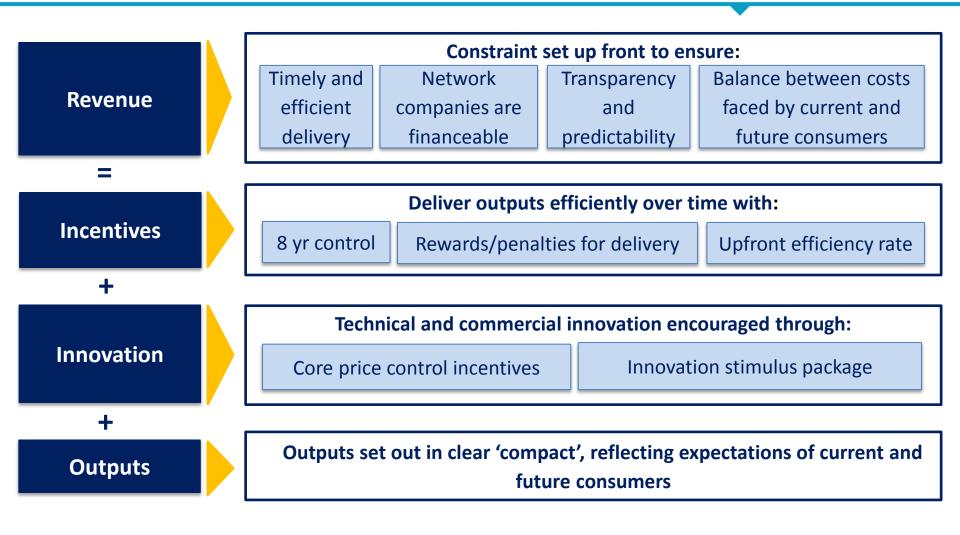
80% down 1990 -2050 (de-carbonise electricity sector by 2030 aim)

Security of supply
Capacity margins reduced in short term

As networks get smarter, regulation needs to be smarter



RIIO - A New Approach to Network Regulation





RIIO – A New Approach

Builds on RPI-X but:

- Focus on company business plans
- Outputs agreed after consultation with customers and other stakeholders
- Strong financial incentives calibrated to ensure financeability
- Encourages longer term planning
- Encourages innovation
- "Fast track" option financial incentive to produce good quality business plans



Alternative Approaches

- Competition in distribution connections
- Offshore transmission competitive tendering
 - Introduced in 2009
 - Investments totalling £2.2bn tendered
- Onshore transmission "Strategic Wider Works"
 - Caithness Moray £1bn project approved January 2015
- Onshore transmission potential introduction of competition
 - Large, separable projects
 - Projects not already allowed for in price control



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